MANUAL OF REGULATIONS

FOR NON-BANK FINANCIAL INSTITUTIONS

Volume 1

FOREWORD

The *2010 Manual of Regulations for Non-Bank Financial Institutions* (MORNBFI) is an updated compilation of regulations and policies issued by the Bangko Sentral ng Pilipinas (BSP) for financial institutions under its supervision. Available in hard and soft copies, it is a convenient reference and guide for said financial institutions in the conduct of their operations.

The updated MORNBFI incorporates regulatory policies issued to align banking practices on risk management, good corporate governance, capital adequacy, accounting and reporting with international standards. It also includes rules implementing legislative reform measures, the more significant of which are the *General Banking Law of 2000*, the *Anti-Money Laundering Act of 2001* and the *Special Purpose Vehicle Act of 2002*.

In providing easy access to this information, the updated MORNBFI seeks to facilitate compliance with the supervisory and regulatory requirements of BSP that will contribute to the enhancement of its partnership with financial institutions under its supervision, and ultimately to the strengthening of the Philippine Banking System and the economy.

AMANDO M. TETANGCO, JR.
Governor

PREFACE
(2010 Edition)

The 2010 Manual of Regulations for Non-Bank Financial Institutions (MORNBFI) is the latest updated edition from the initial issuance in 1996 . The updates consist of the significant policy developments and changes in statutory laws. It shall serve as the principal source of banking regulations issued by the Monetary Board and the Governor of the BSP and shall be cited as the authority for enjoining compliance with the rules and regulations embodied therein.

To accomplish the work of proposing revision to the Old Manual, the Monetary Board of the BSP, in its Resolution No. 1203 dated December 7, 1994, directed the creation of a multi-departmental Ad Hoc Review Committee. The Committee was officially constituted under Office Order No. 2 Series of 1995 and was reconstituted several times thereafter. Under the aforesaid office order, the Committee is tasked to update the Manuals on a continuing basis (i) to incorporate relevant issuances (ii) propose revision/deletion of provisions which have become obsolete, redundant, irrelevant or inconsistent with laws/regulations (iii) reformulate provisions as the need arises and (iv) oversee printing of the Manuals/ Updates in coordination with the Corporate Affairs Office.

The present Committee, as reconstituted under Office Order No. 0152, Series of 2011 dated 01 February 2011, is composed of: Mr. Alberto A. Reyes, Director, Examination Department II (ED) II, Chairman; Atty. Magdalena D. Imperio, Deputy Director, Office of the General Counsel and Legal Services (OGCLS), Vice Chairman; Ms. Ma. Belinda G. Caraan, Deputy Director/Head, Financial Consumer Affairs Group (FCAG); Ms. Ma. Corazon T. Alva, Acting Deputy Director, Examination Department (ED) I; Atty. Lord Eileen S. Tagle, Legal Officer III, OGCLS; Atty. Florabelle S. Madrid, Manager, CPCD I; Ms. Celedina P. Garbosa, Acting Manager, CPCD II; Atty. Asma A. Panda, Legal Officer IV, OGCLS; Ms. Concepcion A. Garcia, Bank Officer IV, ED III; Ms. Ma. Corazon B. Bilgera, Bank Officer II, Anti-Money Laundering Specialists Group (AMLSG), members; and Mr. Nestor A. Espenilla, Jr., Deputy Governor, Supervision and Examination Sector, Adviser.

The Committee Secretariat is headed by Ms. Ma. Cecilia U. Contreras, Supervision and Examination Specialist I, ED II.

The Bangko Sentral ng Pilipinas

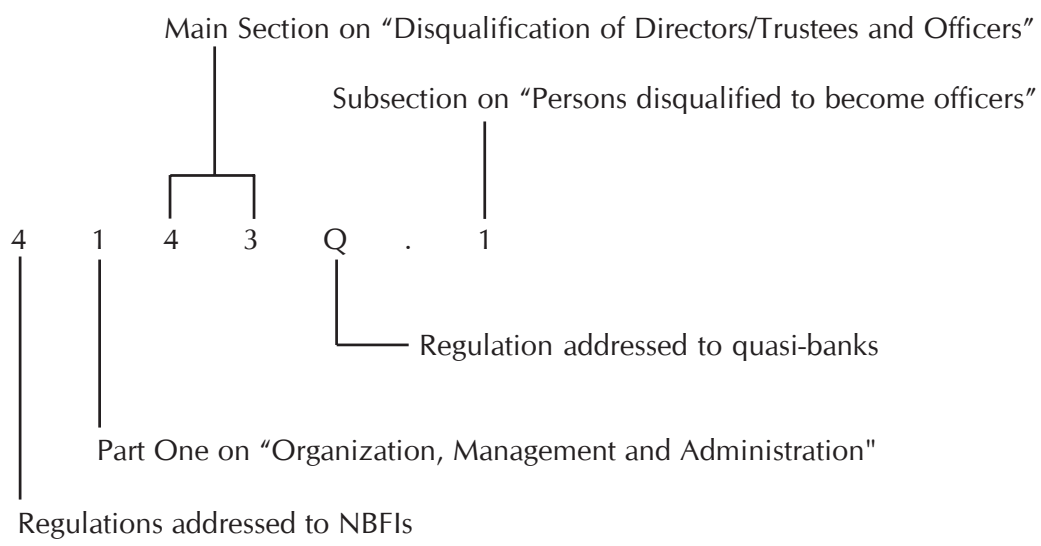
INSTRUCTIONS TO USERS
(2010 Edition)

The Manual of Regulations for Non-Bank Financial Institutions (the "Manual") contains the rules and regulations which govern non-bank financial institutions (NBFIs) subject to the supervision of the Bangko Sentral ng Pilipinas (BSP) under existing laws, i.e. : Quasi-banks (Q Regulations), NSSLAs (S Regulations), Pawnshops (P Regulations), and other NBFIs, trust entities, subsidiaries and affiliates of banks and quasi-banks (N Regulations).

The Manual is divided into four (4) books Q, S, P or N. Each book is divided into parts. Each part is divided into sections containing four (4) digits and the letter Q, S, P or N, as applicable, i.e., 4143Q. The first digit "4" means that the regulation is applicable to NBFIs; the second digit "1" refers to the Part number, and the third and fourth digits "4" and "3" refer to the section number.

Sections may contain subsections represented by number/s after the decimal point, i.e., 4143Q.1.

To illustrate, Subsection 4143Q.1 indicates:



The runners in the upper-right or left hand corners of each page show the sections/ subsections of the regulations and the cut-off date of the regulatory issuances included in the page of the Manual where the runner is shown.

Q REGULATIONS
(Regulations Governing Non-Bank Financial Institutions
Performing Quasi-Banking Functions)

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POWER OF THE BANGKO SENTRAL TO EXAMINE QUASI-BANKS

(2008 - 4654Q) Examination by the Bangko Sentral. The BSP shall have supervision over, and conduct periodic or special examinations of QBs, including their subsidiaries and affiliates in allied activities.

The head and examiners of the appropriate department of the Supervision and Examination Sector (SES) are authorized to administer oaths to any director, officer, or employee of QBs, including their subsidiaries and affiliates engaged in allied activities, and to compel the presentation of all books, documents, papers or records necessary in their judgment to ascertain the facts relative to the true condition of the institution as well as the books and records of persons and entities relative to or in connection with the operations, activities or transactions of the institution under examination, subject to the provision of existing laws protecting or safeguarding the secrecy or confidentiality of investments of private persons, natural or juridical, in debt instruments issued by the Government.

(2008 - 4654Q.1) Definitions

a. *Subsidiary* is a corporation more than fifty percent (50%) of the outstanding voting stock of which is directly or indirectly owned, controlled, or held with power to vote by a QB.

b. *Affiliate* is an entity linked directly or indirectly to a QB by means of:

(1) Ownership, control or power to vote, of ten percent (10%) or more of the outstanding voting stock of the entity, or vice-versa;

(2) Interlocking directorship or officership;

(3) Common stockholders owning ten percent (10%) or more of the outstanding voting stock of each of the financial intermediary and the entity;

(4) Management contract or any arrangement granting power to the financial intermediary to direct or cause the direction of management and policies of the entity, or vice-versa; or

(5) Permanent proxy or voting trust in favor of the financial intermediary constituting ten percent (10%) or more of the outstanding voting stock of the entity, or vice-versa.

c. *Financial allied undertakings* refer to enterprises or firms with homogeneous or similar activities/business/functions with the financial intermediary and may include, but not limited to, leasing companies, banks, IHs, financing companies, credit card operations, FIs addressed/catering to small and medium scale industries, and such other similar activities as the Monetary Board may declare as appropriate from time to time.

d. *Non-financial allied undertakings* may include, but not limited to, warehousing companies, storage companies, safe deposit box companies, companies engaged in the management of mutual funds but not in the mutual funds themselves, management corporations engaged or to be engaged in activities similar to the management of mutual funds, insurance agencies, companies engaged in home building and home development and companies providing drying and/or including facilities for agricultural crops such as rice and corn and such other similar activities as the Monetary Board may declare as appropriate from time to time.

e. **(2008 - 4661Q)** Effective 14 August 2004 the term "*examination*" shall, henceforth, refer to an investigation of an institution under the supervisory authority

of the BSP to determine compliance with laws and regulations. It shall include determination that the institution is conducting its business on a safe and sound basis. Examination requires full and comprehensive looking into the operations and books of institutions, and shall include, but need not be limited to, the following:

(1) Determination of the QB's solvency and liquidity position;

(2) Evaluation of asset quality as well as determination of sufficiency of valuation reserves on loans and other risk assets;

(3) Review of all aspects of QB operations;

(4) Assessment of risk management system, including the evaluation of the effectiveness of the QB management's oversight functions, policies, procedures, internal control and audit;

(5) Appraisal of overall management of the QB;

(6) Review of compliance with applicable laws, rules and regulations; and

(7) Any other activities relevant to the above.

Regular or periodic examination shall be done once a year, with an interval of twelve (12) months from the last date thereof. Special examination may be conducted earlier, or at a shorter interval, when authorized by the Monetary Board by an affirmative vote of five (5) members.

In the full exercise of the supervisory powers of the BSP, examination by the BSP of institutions shall be complemented by overseeing thereof. In this regard, the term *overseeing* shall refer to a limited investigation of an institution, or any investigation/s that is limited in scope, conducted to inquire into a particular area/ aspect of an institution's operations, for the purpose of overseeing that laws and regulations are complied with, inquiring into the solvency and liquidity of the institution, enforcing prompt corrective action, or such other matters requiring immediate investigation: *Provided*, That (i) specific authorizations be issued by the Deputy Governor, SES, and (ii) periodic summary reports on overseeings made be submitted to the Monetary Board.

(Circular No. 442 dated 20 July 2004)

PART ONE

ORGANIZATION, MANAGEMENT AND ADMINISTRATION

A. SCOPE OF AUTHORITY

Section 4101Q Quasi-Banking Functions *Quasi-banking functions* consist of the following:

a. Borrowing funds for the borrower's own account;

b. Twenty (20) or more lenders at any one time;

c. Methods of borrowing: issuance, endorsement, or acceptance of debt instruments of any kind, other than deposits, such as:

(1) acceptances;

(2) promissory notes;

(3) participations;

(4) certificates of assignment or similar instruments with recourse;

(5) trust certificates;

(6) repurchase (repo) agreements; and

(7) such other instruments as the Monetary Board may determine; and

d. Purpose:

(1) relending; or

(2) purchasing receivables or other obligations.

As used in the definition of *quasi-banking functions,* the following terms and phrases shall be understood, as follows:

Borrowing shall refer to all forms of obtaining or raising funds through any of the methods and for any of the purposes provided in Items *"c"* and *"d"* above, whether the borrower's liability thereby is treated as real or contingent.

For the borrower's own account shall refer to the assumption of liability in one's own capacity and not in representation, or as an agent or trustee, of another.

Purchasing of receivables or other obligations shall refer to the acquisition of claims collectible in money, including interbank borrowings or borrowings between financial institutions (FIs), or of securities, of any amount and maturity, from domestic or foreign sources.

Relending shall refer to the extension of loans by an institution with antecedent borrowing transactions. Relending shall be presumed in the absence of express stipulation, when the institution is regularly engaged in lending.

Regularly engaged in lending shall refer to the practice of extending loans, advances, discounts or rediscounts as a matter of business, i.e., continuous or consistent lending as distinguished from isolated lending transactions.

§ 4101Q.1 *Financial intermediaries* *Financial intermediaries* shall mean persons or entities whose principal functions include the lending, investing or placement of funds or evidences of indebtedness or equity deposited with them, acquired by them, or otherwise coursed through them either for their own account or for the account of others.

Principal shall mean chief, main, most considerable or important, of first importance, leading, primary, foremost, dominant or preponderant, as distinguished from secondary or incidental.

Functions shall mean actions, activities or operations of a person or entity by which his/its business or purpose is fulfilled or carried out. The business or purpose of a person or entity may be determined from the purpose clause in its articles of incorporation/partnership, and from the nature of the business indicated in his/its application for registration of business filed with the appropriate government agency.

To be considered a financial intermediary, a person or entity must perform any of the following functions on a regular and recurring, not on an isolated basis:

a. Receive funds from one (1) group of persons, irrespective of number, through traditional deposits, or issuance of debt or equity securities; and make available/lend these funds to another person or entity, and in the process acquire debt or equity securities;

b. Use principally the funds received for acquiring various types of debt or equity securities;

c. Borrow against, or lend on, or buy or sell debt or equity securities;

d. Hold assets consisting principally of debt or equity securities such as promissory notes, bills of exchange, mortgages, stocks, bonds, and commercial papers;

e. Realize regular income in the nature of, but need not be limited to, interest, discounts, capital gains, underwriting fees, guarantees, fees, commissions, and service fees, principally from transactions in debt or equity securities or by being an intermediary between suppliers and users of funds.

Non-banking financial intermediaries shall include the following:

(1) A person or entity licensed and/or registered with any government regulatory body as a non-bank financial intermediary, such as investment house (IH), investment company, financing company, securities dealer/broker, lending investor (IH), pawnshop, money broker, fund manager, cooperative, insurance company, non-stock savings and loan association (NSSLA) and building and loan association.

(2) A person or entity which holds itself out as a non-banking financial intermediary, such as by the use of a business name, which includes the term *financing, finance, investment, lending* and/or any word/phrase of similar import which connotes financial intermediation, or an entity which advertises itself as a financial intermediary and is engaged in the function(s) where financial intermediation is implied.

(3) A person or entity performing any of the functions enumerated in Items *"a"* to *"e"* of this Subsection.

§ 4101Q.2 ***Guidelines on lender count.*** The following guidelines shall govern lender count on borrowings or funds mobilized by non-bank financial intermediaries:

a. For purposes of ascertaining the number of lenders/placers to determine whether or not a non-bank financial intermediary is engaged in quasi-banking functions, the names of payees on the face of each debt instrument shall serve as the primary basis for counting the lenders/placers except when proof to the contrary is adduced such as the official receipts or documents other than the debt instrument itself. In such case the actual/real lenders/placers as appearing in such proof, shall be the basis for counting the number of lenders/placers.

In a debt instrument issued to two (2) or more named payees under an *and/or* and *or* arrangement, the number of payees appearing on the instrument shall be the basis for counting the number of lenders/ placers: *Provided, however,* That a debt instrument issued in the name of a husband and wife followed by the word spouses, whether under an *and, and/or* or *or* arrangement or in the name of a designated payee under an *in trust for* (ITF) arrangement, shall be counted as one (1) borrowing/placement.

b. Each debt instrument payable to bearer shall be counted as one (1) lender/placer except when the non-bank financial intermediary can prove that there is only one (1) owner for several debt instruments so payable.

c. Two (2) or more debt instruments issued to the same payee, irrespective of the date and amount shall be counted as one (1) borrowing or placement.

d. Debt instruments underwritten by IHs or traded by securities dealers/brokers whether on a firm, standby or best efforts basis shall be counted on the basis of the number of purchasers thereof and shall not be treated as having been issued solely to the underwriter or trader: *Provided, however,* That in case of unsold debt instruments in a firm commitment underwriting, the underwriter shall be counted as a lender.

e. Each buyer, assignee, and/or indorsee shall be counted in determining the number of lenders/placers of funds mobilized through sale, assignment, and/or indorsement of securities, or receivables on a without recourse basis, whenever the terms and/or attendant documentation, practice, or circumstances indicate that the sale, assignment, and/or indorsement thereof legally obligates the non-bank financial intermediary to repurchase or reacquire the securities/ receivables sold, assigned, indorsed or to pay the buyer, assignee, or indorsee at some subsequent time.

f. Funds obtained by way of advances from stockholders, directors, officers, regardless of nature, shall be considered borrowed funds or funds mobilized and such stockholders, directors or officers shall be counted in determining the number of lenders/placers.

§ 4101Q.3 *Transactions not considered quasi-banking.* The following shall not constitute quasi-banking:

a. Borrowing by commercial, industrial and other non-financial companies, through the means listed in Sec. 4101Q for the limited purpose of financing their own needs or the needs of their agents or dealers; and

b. The mere buying and selling without recourse of instruments mentioned in Sec. 4101Q: *Provided,* That:

(1) The institution selling without recourse shall indicate or stamp in conspicuous print on the instrument/s, as well as on the confirmation of sale (COS), the phrase *without recourse* or *sans recourse* and the following statement:

(Name of financial intermediary) assumes no liability for the payment, directly or indirectly, of this instrument.

(2) In the absence of the phrase *without recourse* or *sans recourse* and the above- required accompanying statement, the instrument so issued, endorsed or accepted shall automatically be considered as falling within the purview of the rules on quasi-banking.

Provided, further, That any of the following practices or practices similar and/ or tantamount thereto in connection with a without recourse transaction renders such transaction as with recourse and within the purview of the rules on quasi-banking.

(i) Issuance of postdated checks by a financial intermediary, whether for its own account or as an agent of the debt instrument issuer, in payment of the debt instrument sold, assigned or transferred without recourse;

(ii) Issuance by a financial intermediary of any form of guaranty on sale transactions or on negotiations or assignment of debt instruments without recourse; or

(iii) Payment with the funds of the financial intermediary which assigned, sold or transferred the debt instrument without recourse, unless the financial intermediary can show that the issuer has with the said financial intermediary funds corresponding to the amount of the obligation.

Any IH violating the provisions of this Subsection shall be subject to the sanctions provided in Sections 12 and 16 of P.D. No. 129, as amended.

§ 4101Q.4 *Delivery of securities* [1]

a. Securities sold *on a without recourse basis* allowed under Subsec. 4101Q.3(b) shall be delivered physically to the purchaser, or to his designated custodian duly accredited by the BSP, if certificated, or by means of book-entry transfer to the appropriate securities account of the purchaser or his designated BSP accredited custodian in a registry for said securities, if immobilized or dematerialized, while the COS or document of conveyance by the seller shall be physically delivered to the purchaser. The custodian shall hold the securities in the name of the buyer: *Provided,* That a QB/other entity authorized by the BSP to perform custodianship function may not be allowed to be custodian of securities issued or sold on a without recourse basis by said non-bank financial institution (NBFI), its subsidiaries or affiliates, or of securities in bearer form.

The delivery shall be effected upon payment and shall be evidenced by a securities delivery receipt duly signed by the authorized officer of the custodian and delivered to the purchaser.

Sanctions. Violation of any provision of this Subsection shall be subject to the following sanctions/penalties:

(1) *Monetary penalties*

First offense - Fine of P10,000 a day for each violation reckoned from the date the violation was committed up to the date it was corrected.

Subsequent offenses - Fine of P20,000 a day for each violation reckoned from the date the violation was committed up to the date it was corrected.

(2) *Other sanctions*

First offense - Reprimand for the directors/officers responsible for the violation.

Subsequent offense -

(a) Suspension for ninety (90) days without pay of directors/officers responsible for the violation;

(b) Suspension or revocation of the accreditation to perform custodianship function;

(c) Suspension or revocation of the authority to engage in quasi-banking function; and/or

(d) Suspension or revocation of the authority to engage in trust and other fiduciary business.

b. The guidelines to implement the delivery by the seller of securities to the buyer or to his designated third party custodian are shown in *Appendix Q-38*.

Sanctions. Without prejudice to the penal and administrative sanctions provided for under Sections 36 and 37, respectively of R.A. No. 7653 (The New Central Bank Act), violation of any provision of the guidelines in *Appendix Q-38* shall be subject to the following sanctions/penalties depending on the gravity of the offense:

(a) *First offense* -

(1) Fine of up to P10,000 a day for the institution for each violation reckoned from the date the violation was committed up to the date it was corrected; and

(2) Reprimand for the directors/officers responsible for the violation.

(b) *Second offense* -

(1) Fine of up to P20,000 a day for the institution for each violation reckoned from the date the violation was committed up to the date it was corrected; and

(2) Suspension for ninety (90) days without pay of directors/officers responsible for the violation.

(c) *Subsequent offenses* -

(1) Fine of up to P30,000 a day for the institution for each violation from the date the violation was committed up to the date it was corrected;

(2) Suspension or revocation of the authority to act as securities custodian and/or registry; and

(3) Suspension for 120 days without pay of the directors/officers responsible for the violation.

(As amended by M-2007-002 dated 23 January 2007, M-2006-009 dated 18 July 2006, M-2006-002 dated 05 June 2006 and Circular No. 524 dated 31 March 2006)

[1] Effective 16 November 2004 under Circular 450 dated 06 September 2004.

§ 4101Q.5 *Securities custodianship operations*

a. Securities sold *on a without recourse basis* shall be delivered to the purchaser, or to his designated custodian duly accredited by the BSP: *Provided* , That a bank/other entity authorized by the BSP to perform custodianship function may not be allowed to be custodian of securities issued or sold on a without recourse basis by said QB/entity, its subsidiaries or affiliates, or of securities in bearer form. Existing securities being held under custodianship by QB/other entities under BSP supervision, which are not in accordance with said regulation, must therefore, be delivered to a BSP accredited third party custodian. However, banks and other FIs under BSP supervision may maintain custody of existing securities of their clients who are unable or unwilling to take delivery pursuant to the provisions of this Subsection but who declined to deliver their existing securities to a BSP accredited third party custodian subject to the following conditions:

(1) the custody arrangements with clients have been in existence prior to 05 November 2004 (effectivity date of Circular No. 457 dated 14 October 2004);

(2) the dealing bank/NBFI under BSP supervision had been informed in writing by the client that he is not willing to have his existing securities delivered to a third party custodian;

(3) any BSP regulated institution shall not enter into securities transactions with a client who has outstanding securities not delivered to a BSP accredited third party custodian; and

(4) it shall be the responsibility of any BSP regulated institution to satisfy itself that the person purchasing securities from it has no outstanding securities holdings which were not delivered to a BSP accredited third party custodian.

b. *Sanctions*. Without prejudice to the penal and administrative sanctions provided for under Sections 36 and 37, respectively, of R.A. No. 7653, violation of any provision of this Subsection shall be subject to the following sanctions/penalties:

(1) *First offense* -

(a) Fine of up to P10,000 a day for the institution for each violation reckoned from the date the violation was committed up to the date it was corrected; and

(b) Reprimand for the directors/officers responsible for the violation.

(2) *Second offense* -

(a) Fine of up to P20,000 a day for the institution for each violation reckoned from the date the violation was committed up to the date it was corrected; and

(b) Suspension for ninety (90) days without pay of directors/officers responsible for the violation.

(3) *Subsequent offenses* -

(a) Fine of up to P30,000 a day for the institution for each violation from the date the violation was committed up to the date it was corrected;

(b) Suspension or revocation of the authority to act as securities custodian and/or registry; and

(c) Suspension for 120 days without pay of the directors/officers responsible for the violation.

§ 4101Q.6 *Sale, discounting, assignment or negotiation by quasi-banks of their credit rights arising from claims against the Bangko Sentral to clients.* Pursuant to the policy of the BSP to promote investor protection and transparency in securities transactions as important components of capital markets development, credit rights in Special Deposit Account (SDA) placements and reverse repo agreements with the BSP, shall not be the subject of sale, discounting, assignment or negotiation on a with or without recourse basis.

Any violation of the provisions of this Subsection shall be considered a less serious offense and shall subject the QB and

the director/s and/or officer/s concerned to the sanctions provided under Sec. 4199Q.
(Circular No. 636 dated 17 December 2008)

§ 4101Q.7 ***(2008 - 4655Q) Applicability of rules governing universal banks to quasi-banks.*** In case of conflict between rules applicable to banks with universal banking authority and those applicable to QBs in activities where they perform the same functions, the rules governing banks with universal banking authority shall prevail.

B. ESTABLISHMENT AND ORGANIZATION

Sec. 4102Q Statement of Policy. It is the policy of the BSP to promote the development of the domestic financial market so as to foster a sound, efficient and inclusive financial system fully supportive of sustainable economic growth. Towards this end, the grant of authority to engage in quasi-banking functions to IHs and finance companies shall be allowed subject to the following conditions:

a. That quasi-banking activities shall be undertaken by the institution concerned to pursue its core business, i.e., underwriting of securities of other corporations and of the government or its instrumentalities, participating as soliciting dealer or selling group member in tender offers, block sales, or exchange offering of securities, and dealing in options, rights or warrants relating to securities and such other powers which a dealer may exercise under the Securities Regulation Code (SRC), in the case of IHs, and discounting or factoring commercial papers or accounts receivable, or by buying and selling contracts, leases, chattel mortgages (CHMs), or other evidences of indebtedness, or by leasing of motor vehicles, heavy equipment and industrial machinery, business and office machines and equipment, appliances and other movable property, or granting business and consumer loans, in the case of finance companies;

b. That the institution concerned shall fully inform investors of the nature of a deposit substitute instrument, e.g., that it is not covered by the Philippine Deposit Insurance Corporation (PDIC), that pre-termination thereof is subject to penalty, where applicable, and such other material risks involved in investing in such instrument; and

c. That the institution concerned shall conduct effective investor suitability testing procedures.
(Circular No. 557 dated 12 January 2007)

§ 4102Q.1 ***Preconditions for the exercise of quasi-banking functions.*** No person or entity shall engage in quasi-banking functions without authority from the BSP. Only a duly incorporated IH and finance company may undertake or perform quasi-banking functions as defined in Section 4101Q. An institution securing BSP authority to engage in quasi-banking functions must meet the following requirements:

a. It must have complied with the minimum adjusted capital accounts of at least P300.0 million or such amounts as may be required by the Monetary Board in the future;

b. It has generally complied with applicable laws, rules and regulations, orders or instructions of appropriate authority, including the Monetary Board and/or BSP Management where applicable;

c. Its accounting records, systems and procedures as well as internal control systems are satisfactorily maintained;

d. It does not have float items outstanding for more than sixty (60) calendar days in the "Due From/To Head Office/Branches/Offices" accounts exceeding one percent (1%) of the total resources as of end of preceding month;

e. It has no past due obligation with any FI as of date of application;

f. The officers who will be in-charge of the quasi-banking operations have actual experience of at least two (2) years in a bank or QB as in-charge (or at least as assistant-in-charge). The directors of the institution, officer-in-charge of the quasi-banking operations and the managerial staff must comply with the fit and proper rule prescribed under existing law/rules and regulations;

g. The institution has elected at least two (2) independent directors and all its directors have attended the required seminar for directors of QBs conducted or accredited by the BSP;

h. It has not engaged in unsafe and unsound practices during the past six (6) months immediately preceding the date of application where applicable;

i. It must have in place a comprehensive risk management system approved by its board of directors appropriate to its operations characterized by a clear delineation of responsibility for risk management, adequate risk measurement systems, appropriately structured risk limits, effective internal control and complete, timely and efficient risk reporting systems. In this connection, a manual of operations and other related documents embodying the risk management system must be submitted to the appropriate department of the Supervision and Examination Sector (SES) at the time of application for authority and within thirty (30) days from updates.

(As amended by Circular No. 557 dated 12 January 2007)

Sec. 4103Q Application for a Certificate of Authority from the Bangko Sentral[1]. An institution securing BSP's Certificate of Authority to engage in quasi-banking functions shall file an application with the appropriate department of the SES. The application shall be signed by the president or officer of equivalent rank of the institution and shall be accompanied by the following documents:

a. Certified true copy of the resolution of the board of directors of the institution authorizing the application;

b. A certification signed by the president or officer of equivalent rank that:

(1) the institution has complied with all conditions/prerequisites for the grant of authority to engage in quasi-banking functions;

(2) quasi-banking functions shall be pursued/undertaken by the institution in the furtherance of its core business, e.g., underwriting of and dealing in securities of other corporations and of the government or its instrumentalities, in the case of IHs, and leasing and/or discounting/factoring commercial papers or accounts receivable, or granting business and consumer loans, in the case of finance companies;

(3) investors shall be informed that their investments/placements are not insured by the PDIC and that any pre-termination thereof shall be subject to penalty, if applicable, as well as all other material risks; and

(4) investors shall be subjected to effective investor suitability testing procedures;

c. An information sheet;

d. Bio-data signed under oath, of the members of the managerial staff who will undertake quasi-banking operations; and

e. Borrowing-investment program for one (1) year, and annually thereafter on or before November 30, which should include at the minimum:

(1) planned distribution of portfolios as to:

(a) underwriting;
(b) commercial papers;
(c) stocks and bonds;
(d) government securities(GS);
(e) receivables financing, discounting and factoring;
(f) leasing; and
(g) direct loans;

(2) expected sources of funds to support investment program classified as to:

(a) maturity: short, medium and long-term;

[1] See SEC Circular Nos. 5 dated 17 July 2008, 3 dated 16 February 2006 and 14 dated 24 October 2000.

(b) interest rates; and

(c) domestic or foreign sources whether institutional or personal.

The foregoing requirement shall also apply to QBs existing as of 03 February 2007.

Transitory provisions. IHs and finance companies authorized to engage and are actually performing quasi-banking functions but do not meet the new capital requirement are hereby given a period of two (2) years reckoned from 03 February 2007 within which to comply with the minimum capital requirement in Subsec. 4102Q.1(a): *Provided,* That this may be substituted by a capital build-up program for a period of not more than three (3) years which must be approved by the Monetary Board. Such capital build-up program shall be in equal annual or diminishing amounts; and shall be submitted to the appropriate department of the SES within three (3) months from 03 February 2007. QBs which fail to comply with the required capitalization upon expiration of said two (2) year period given them or those which fail to comply with the approved capital build-up program shall liquidate their quasi-banking operations within one (1) year from said deadlines and their licenses shall be considered revoked/cancelled.

The licenses of existing QBs not actually performing quasi-banking functions which do not meet the required minimum capitalization provided in Subsec. 4102Q.1(a) on 03 February 2007 shall be automatically revoked.

(As amended by CL-2008-078 dated 15 December 2008, CL-2008-053 dated 21 August 2008, CL-2008-007 dated 05 February 2008 and Circular No. 557 dated 12 January 2007)

Sec. 4104Q Issuance of Bangko Sentral Certificate of Authority. The BSP shall issue a Certificate of Authority upon proof that the applicant has complied with the requirements of Secs. 4102Q and 4103Q and of pertinent laws and regulations.

In the case of a merger or consolidation of two (2) or more QBs, the authority shall continue to have full force and effect. For documentation purposes, in the case of a merger, the Certificate of Authority of the absorbing corporation shall be maintained; and with respect to consolidation, a new certificate shall be issued to the new corporation. The Certificate of Authority of the absorbed corporation in a merger and the certificates of the consolidated corporations in a consolidation shall be surrendered to the appropriate department of the BSP.

Sec. 4105Q Licensing of an Investment House. Applications for license as an IH referred to the BSP by the Securities and Exchange Commission (SEC) pursuant to P.D. No. 129 shall be evaluated in accordance with the Guidelines to Evaluate Investment Houses prescribed in *Appendix Q-1*.

Sec. 4106Q *(2008 - 4656Q)* Basic Laws Governing Investment Houses and Financing Companies. The following are the basic laws governing investment houses (IHs) and financing companies:

a. *IHs*. P.D. No. 129, as amended, known as *The Investment Houses Law,* governs the establishment, operation and regulation of IHs. To effectively carry out the provisions of this Decree, the SEC, pursuant to the powers vested in it by said Decree, promulgated basic rules and regulations *(Appendix Q-18)* to implement the provisions of the Decree.

b. *Financing companies*. R.A. No. 8556, known as *The Financing Company Act of 1998*, regulates the organization and operation of financing companies. To effectively carry out the provisions of this Act, the SEC, pursuant to the powers vested in it under said Act, promulgated basic rules and regulations to implement the provisions of the Act *(Appendix Q-19)*.

Sec. 4107Q (Reserved)

C. MERGER/CONSOLIDATION

Sec. 4108Q *(2008 - 4111Q)* Merger/ Consolidation Involving Quasi-Banks. The merger/ consolidation of QBs is encouraged to meet minimum capital requirements and to develop larger and stronger FIs. QBs which are IHs are likewise encouraged to merge with banks to obtain authority to perform expanded commercial banking functions.

Mergers/consolidations involving QBs shall comply with the provisions of applicable law and shall be subject to approval by the BSP.

For purposes of merger and consolidation of QBs, the following definitions shall apply:

a. *Merger* is the absorption of one (1) or more corporations by another existing corporation, which retains its identity and takes over the rights, privileges, franchises, and properties, and assumes all the liabilities and obligations of the absorbed corporation(s) in the same manner as if it had itself incurred such liabilities or obligations. The absorbing corporation continues its existence while the life or lives of the other corporation(s) is/are terminated.

b. *Consolidation* is the union of two(2) or more corporations into a single new corporation, called the consolidated corporation, all the constituent corporations thereby ceasing to exist as separate entities. The consolidated corporation shall thereupon and thereafter possess all the rights, privileges, immunities, franchises and properties, and assume all the liabilities and obligations of each of the constituent corporations in the same manner as if it had itself incurred such liabilities or obligations.

§ 4108Q.1 *Requirement of Bangko Sentral approval.* Mergers and consolidations involving QBs shall comply with the provisions of applicable law and shall be subject to approval by the BSP.

The guidelines and procedures in the application for merger/consolidation as shown in *Appendix Q*-51 shall be observed by QBs.

(M-2009-028 dated 12 August 2009)

§ 4108Q.2 *(Reserved)*

§ 4108Q.3 *(2008 - 4112Q) Merger/ consolidation incentives.* In pursuance of the policy to promote mergers and consolidations among banks and other financial intermediaries as a means to develop larger and stronger FIs, constituent entities may, subject to BSP approval, avail themselves of any or all of the following incentives:

a. Revaluation of premises, improvements and equipment of the institutions: *Provided,* That such revaluation shall be based on fair valuation of the property conducted by a reputable appraisal company which shall be subject to review and approval by the BSP

The following rules shall govern the revaluation of assets:

(1) The revaluation of the QB's premises, improvements and equipment shall be allowed only to all institutions participating in a merger/consolidation if all of them belong to the same category, or at least two (2) of them belong to the highest category among the merging/ consolidating institutions.

(2) In case the merging/consolidating institutions do not belong to the same category or only one (1) of them falls under the highest category, all of them may be allowed to revalue their premises, improvements and equipment: *Provided*, That the amount of appraisal increment resulting from such revaluation shall be limited to the amount of the total resources of the institution belonging to the lower category or categories.

(3) The appraisal increment resulting from the revaluation shall form part of capital

for purposes of determining the single borrower's limit and capital-to-risk assets ratio. The use of appraisal increment for cash dividend shall be governed by the provisions of the Corporation Code.

(4) The revaluation of premises, improvements, and equipment of the institution as well as the recognition of goodwill as an incentive to mergers/ consolidations shall only be allowed if the following conditions are met:

(i) The surviving or consolidated entity will meet the existing capital requirements after all adjustments are taken up in the books of accounts of the merging/ consolidating entities but before considering appraisal increments and goodwill, or there will be infusion of fresh capital to meet said existing capital requirements; and

(ii) The merger/consolidation will result in a more viable FI as a result of cost savings and improve competitive position.

In case of purchase or acquisition of the majority or all of the outstanding shares of stock of a QB, the same conditions must be satisfied.

b. Unbooked valuation reserves based upon BSP examination and other capital adjustments resulting from the merger/ consolidation may be booked on staggered basis over a maximum period of five (5) years.

The following guidelines shall govern the staggered booking of valuation reserves:

(1) The booking on staggered basis over a maximum period of five (5) years of unbooked valuation reserves based upon examination by the BSP may be allowed to all institutions participating in a merger/ consolidation if all of them belong to the same category, or at least two (2) of them belong to the highest category among the merging/consolidating institutions.

(2) In case the merging/consolidating institutions do not belong to the same category or only one (1) of them falls under the highest category, all of them may be allowed to book the required valuation reserves based upon examination by the BSP on a staggered basis over a maximum period of five (5) years: *Provided,* That the aggregate amount of the required valuation reserves shall be limited to the amount of the total resources of the institution belonging to the lower category or categories.

c. If by reason of merger/ consolidation, the resulting QB is unable to comply fully with the prescribed net worth-to-risk assets ratio, the Monetary Board may, at its discretion, temporarily relieve the QB from full compliance with this requirement under such conditions as it may prescribe;

In the case of purchase or acquisition of majority or all of the outstanding shares of a QB by a bank/another QB, the revaluation of assets and the booking of the required valuation reserves based upon examination by the BSP over a period of five (5) years shall be allowed only if such purchase or acquisition is for the purpose of rehabilitating the former QB: *Provided,* That the revaluation of assets and staggered booking of reserves shall be allowed in full only if the purchaser is another QB and both the QBs belong to the same category. Otherwise, only the QB being acquired/ rehabilitated shall be allowed to recognize in full the appraisal increment resulting from revaluation of assets and to book valuation reserves on a staggered basis, while in the case of the acquiring bank/QB, the appraisal increment resulting from revaluation of assets and the privilege of staggered booking of valuation reserves shall each be limited to the amount of the total resources of the QB being acquired/rehabilitated.

d. Conversion or upgrading of the existing head offices, branches and/or other offices of the merged/absorbed institutions into branches of the new or surviving FI;

e. *(Deleted by Cir. No. 494 dated 20 September 2005)*

f. Relocation of branches/offices may be allowed within one (1) year from date of merger/consolidation in cases where the merger/consolidation resulted in duplication of branches/offices in a service area, or in such other cases/circumstances as the Monetary Board may prescribe;

g. Outstanding penalties in legal reserve deficiencies and interest on overdrafts with the BSP as of the date of merger/consolidation may be paid in installments over a period of one (1) year;

h. Restructuring/plan of payment of past due obligations of the proponents with the

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BSP as of the date of merger/consolidation over a period not exceeding ten (10) years;

i. Subject to approval of the Monetary Board, concurrent officerships between a merged/consolidated bank/FI and another bank/FI may be allowed; and

j. Any right or privilege granted a merging bank under a rehabilitation program previously approved by the Monetary Board or under any special authority previously granted by the Monetary Board shall continue to be in effect.

The revaluation of assets and staggered booking of valuation reserves shall be available for a period of two (2) years from 19 February 1999 while the rest of the incentives enumerated under Subsec. 4108Q.3 shall be available for a period of three (3) years from 31 August 1998.

The foregoing incentives may also be granted in cases of purchases or acquisitions of majority or all of the outstanding shares of stock of a QB.

Secs. 4109Q - 4110Q (Reserved)

D. CAPITALIZATION

Sec. 4111Q *(2008 - 4106Q)* Minimum Required Capitalization. A QB shall have a minimum combined capital accounts of ₱300.0 million.

Combined capital accounts shall mean the total of capital stock, retained earnings and profit and loss summary, net of (a) such unbooked valuation reserves and other capital adjustments as may be required by the BSP, (b) total outstanding unsecured credit accommodations, both direct and indirect, to directors, officers, all stockholders and their related interests (DOSRI) and, (c) unsecured loans, other credit accommodations and guarantees granted to subsidiaries and affiliates. With respect to Item *"b"* hereof, the provisions of Sec. 4326Q shall apply except that in the definition of *stockholders* in Subsec. 4326Q.1, the qualification that his stockholdings, individually and/or together with his related interests in the lending QB, amount to ten percent (10%) or more of the total subscribed capital stock of the QB, shall not apply for purposes of this Item. Any appraisal surplus or appreciation credit as a result of appreciation or an increase in book value of the assets of the QB shall be excluded, except in the case of merger and consolidation, where the appraisal increment resulting from the revaluation shall form part of capital for purposes of determining single borrower's limit and capital-to-risk assets ratio.

Any foreign equity shall be registered with and approved by the Board of Investments and the appropriate department of the BSP.
(As amended by Circular No. 560 dated 31 January 2007)

Sec. 4112Q *(2008 - 4107Q)* Minimum Capital of Investment House. The minimum paid-in capital requirement for an IH shall be P300 million pursuant to R.A. No. 129, as amended by R.A. No. 8366.

Secs. 4113Q *(2008 - 4108Q)* Sanctions Any or all of the following sanctions may be imposed on any QB which fails to maintain at least the applicable minimum capital under Secs. 4111Q and 4112Q:

(1) Suspension of authority to engage in quasi-banking functions;

(2) Suspension of authority to engage in trust/investment management activities (in the case of an IH);

(3) Cease-and-desist order (in the case of an IH);

(4) No new/renewal/extension of credit accommodations to DOSRI;

(5) Prohibition against declaration of cash dividends;

(6) Suspension of the privilege to establish and/or open approved branches, agencies, offices, etc.; and

(7) Other sanctions as may be imposed by the Monetary Board.

Sec. 4114Q (Reserved)

E. RISK-BASED CAPITAL

Sec. 4115Q *(2008 - 4116Q)* Basel II Risk-Based Capital. The guidelines implementing the revised riskbased capital adequacy framework for the Philippine banking system to conform to Basel II recommendations is provided in *Appendix Q-46b*. These guidelines apply to all Univeral Banks (UBs) and commercial Banks (KBs), as well as their subsidiary banks and QBs.

The risk-based capital ratio of a QB, expressed as a percentage of qualifying capital to risk-weighted assets, shall not be less than ten percent (10%) for both solo basis (head office plus branches) and consolidated basis (parent QB plus subsidiary financial allied undertakings, but excluding insurance companies).

The ratio shall be maintained daily. This shall be effective 01 January 2004.

(As amended by Circular No. 588 dated 11 December 2007, M-2007-019 dated 21 June 2007, Circular Nos. 560 dated 31 January 2007 and 538 dated 04 August 2006)

§ 4115Q.1 *(2008 - 4116Q) Scope.* The Basel II guidelines apply to all UBs and KBs as well as their subsidiary banks and QBs.

§ 4115Q.2 *(Reserved)*

Sec. 4116Q Basel I Risk-Based Capital The risk-based capital ratio of a QB, expressed as a percentage of qualifying capital to risk-weighted assets, shall not be less than ten percent (10%) for both solo basis (head office plus branches) and consolidated basis (parent QB plus subsidiary financial allied undertakings, but excluding insurance companies).

(As amended by Circular No. 588 dated 11 December 2007, M-2007-019 dated 21 June 2007, Circular Nos. 560 dated 31 January 2007 and 538 dated 04 August 2006)

§ 4116Q.1 *Scope.* QBs that are not subsidiaries of UBs or KBs shall continue to be subject to the risk-based capital adequacy framework, as provided below as well as Subsecs. 4116Q.1 to 4116Q.6.

§ 4116Q.2 *(2008 - 4116Q.1) Qualifying capital.* The qualifying capital shall be the sum of -

a. *Tier 1 (core) capital* -

(1) Paid-up common stock;

(2) Paid-up perpetual and non-cumulative preferred stock;

(3) Common stock dividends distributable;

(4) Perpetual and non-cumulative preferred stock dividends distributable;

(5) Surplus;

(6) Surplus reserves;

(7) Undivided profits; and

(8) Minority interest in the equity of subsidiary financial allied undertakings which are less than wholly-owned: *Provided,* That a QB shall not use minority interests in the equity accounts of consolidated subsidiaries as avenue for introducing into its capital structure elements that might not otherwise qualify as Tier 1 capital or that would, in effect, result in an excessive reliance on preferred stock within Tier 1:

Provided, further, That the following items shall be deducted from the total of Tier 1 capital:

(a) Common stock treasury shares;

(b) Perpetual and non-cumulative preferred stock treasury shares;

(c) Net unrealized losses on underwritten listed equity securities purchased (for IH);

(d) Unbooked valuation reserves and other capital adjustments based on the latest report of examination as approved by the Monetary Board;

(e) Total outstanding unsecured credit accommodations, both direct and indirect, to DOSRI;

(f) Unsecured loans, other credit accommodations and guarantees granted to subsidiaries and affiliates;

(g) Deferred income tax; and

(h) Goodwill.

b. *Tier 2 (supplementary) capital which shall be the sum of* -

(1) *Upper Tier 2 (UT2) capital* -

(a) Paid-up perpetual and cumulative preferred stock;

(b) Perpetual and cumulative preferred stock dividends distributable;

(c) Appraisal increment reserve - QB premises, as authorized by the Monetary Board;

(d) Net unrealized gains on underwritten listed equity securities purchased: *Provided,* That the amount thereof that may be included in UT2 capital shall be subject to a fifty-five percent (55%) discount (for IH);

(e) General loan loss provision: *Provided,* That the amount thereof that may be included in UT2 capital shall be limited to a maximum of one and twenty-five hundredths percent (1.25%) of gross risk-weighted assets, and any amount in excess thereof shall be deducted from the total risk-weighted assets in computing the denominator of the risk-based capital ratio;

(f) With prior BSP approval, unsecured subordinated debt (UnSD) with a minimum original maturity of at least ten (10) years, subject to the following conditions:

(i) It must not be secured nor covered by a guarantee of the issuer or related party;

(ii) It must be subordinated in the right of payment of principal and interest to all creditors of the QB, except those creditors expressed to rank equally with, or behind holders of the debt. Subordinated creditors must waive their right to set off any amounts they owe the QB against subordinated amounts owed to them by the QB. The issue documentation must clearly state that the debt is subordinated;

(iii) It must be fully paid-up. Only the net proceeds actually received from debt issues can be included as capital. If the debt is issued at a premium, the premium cannot be counted as part of capital;

(iv) It must not be redeemable at the initiative of the holder;

(v) It must not contain any clause which requires acceleration of payment of principal, except in the event of insolvency;

(vi) It must not be repayable prior to maturity without the prior consent of the BSP: *Provided*, That repayment may be allowed in connection with call option only after a minimum of five (5) years from issue date and only if – (1) the QB's capital ratio is at least equal to the required minimum capital ratio; and (2) the debt is simultaneously replaced with issues of new capital which is neither smaller in size nor of lower quality than the original issue;

(vii) It may allow a moderate step-up in the interest rate in conjunction with a call option, only if the step-up occurs at a minimum of ten (10) years after the issue date and if it results in an increase over the initial rate that is not more than 100 basis points: *Provided*, That only one (1) rate step up shall be allowed over the life of the instrument;

(viii) It must provide for possible conversion into common shares or preferred shares or possible deferral of payment of principal and interest if the QB's capital ratio becomes less than the required minimum capital ratio;

(ix) It must provide for the principal and interest on the debt to absorb losses where the QB would not otherwise be solvent;

(x) It must allow deferment of interest payment on the debt in the event of, and at the same time as, the elimination of dividends on all outstanding common or preferred stock of the issuer. It is acceptable for the deferred interest to bear interest, but the interest rate payable on deferred interest should not exceed market rates;

(xi) It must be underwritten by a third party not related to the issuer QB nor acting in reciprocity for and in behalf of the issuer QB;

(xii) It must be issued in minimum denominations of at least P500,000 or its equivalent; and

(xiii) It must clearly state on its face that it is not a deposit and is not insured by the PDIC:

Provided, That it shall be subject to a cumulative discount factor of twenty percent (20%) per year during the last five (5) years to maturity [i.e., twenty percent (20%) if the remaining life is four (4) years to less than five (5) years, forty percent (40%) if the remaining life is three (3) years to less than four (4) years, etc.]: *Provided, further,* That where it is denominated in a foreign currency, it shall be revalued periodically (at least monthly) in Philippine peso at prevailing exchange rate using the same exchange rate used for revaluation of foreign currency-denominated assets, liabilities and forward contracts under existing regulations: *Provided furthermore,* That, for purposes of reserve requirement regulation, it shall not be treated as a deposit substitute liability or other forms of borrowings;

(g) Deposit for common stock subscription; and

(h) Deposit for perpetual and non-cumulative preferred stock subscription: *Provided,* That the following items shall be deducted from the total of UT2 capital:

(i) Perpetual and cumulative preferred stock treasury shares;

(2) *Lower Tier 2 (LT2) capital* -

(a) Paid-up limited life redeemable preferred stock: *Provided,* That these shall be subject to a cumulative discount factor of twenty percent (20%) per year during the last five (5) years to maturity [i.e., twenty percent (20%) if the remaining life is four (4) years to less than five (5) years, forty percent (40%) if the remaining life is three (3) years to less than four (4) years, etc.];

(b) Limited life redeemable preferred stock dividends distributable;

(c) With prior BSP approval, UnSD with a minimum original maturity of at least five (5) years, subject to the following conditions:

(i) It must not be secured nor covered by a guarantee of the issuer or related party;

(ii) It must be subordinated in the right of payment of principal and interest to all creditors of the QB, except those creditors expressed to rank equally with, or behind holders of the debt. Subordinated creditors must waive their right to set off any amounts they owe the QB against subordinated amounts owed to them by the QB. The issue documentation must clearly state that the debt is subordinated;

(iii) It must be fully paid-up. Only the net proceeds actually received from debt issues can be included as capital. If the debt is issued at a premium, the premium cannot be counted as part of capital;

(iv) It must not be redeemable at the initiative of the holder;

(v) It must not contain any clause which requires acceleration of payment of principal, except in the event of insolvency;

(vi) It must not be repayable prior to maturity without the prior consent of the BSP: *Provided*, That repayment may be allowed in connection with call option only after a minimum of five (5) years from issue date and only if – (1) the QB's capital ratio is at least equal to the required minimum capital ratio; and (2) the debt is simultaneously replaced with issues of new capital which is neither smaller in size nor of lower quality than the original issue;

(vii) It may allow a moderate step-up in the interest rate in conjunction with a call option, only if the step-up occurs at a minimum of five (5) years after the issue date and if it results in an increase over the initial rate that is not more than 100 basis points or fifty percent (50%) of the initial credit spread, at the option of the bank: *Provided*, That only one (1) rate step up shall be allowed over the life of the instrument;

(viii) It must be underwritten by a third party not related to the issuer QB nor acting

in reciprocity for and in behalf of the issuer QB;

(ix) It must be issued in minimum denominations of at least P500,000 or its equivalent; and

(x) It must clearly state on its face that it is not a deposit and is not insured by the PDIC:

Provided, That it shall be subject to a cumulative discount factor of twenty percent (20%) per year during the last five (5) years to maturity [i.e., twenty percent (20%) if the remaining life is four (4) years to less than five (5) years, forty percent (40%) if the remaining life is three (3) years to less than four (4) years, etc.]: *Provided, further,* That where it is denominated in a foreign currency, it shall be revalued periodically (at least monthly) in Philippine peso using the same exchange rate used for revaluation of foreign currency denominated assets, liabilities and forward contracts under existing regulations: *Provided, finally,* That, for purposes of reserve requirement regulation, it shall not be treated as equivalent to a deposit substitute liability or other forms of borrowings; and

(d) Deposit for perpetual and cumulative preferred stock subscription;

Provided, That the following items shall be deducted from the total of Lower Tier 2 capital:

(1) Limited life redeemable preferred stock treasury shares; and

(2) Sinking fund for redemption of limited life redeemable preferred stock: *Provided*, That the amount to be deducted shall be limited to the balance of redeemable preferred stock after applying the cumulative discount factor:

Provided, further, That the total amount of LT2 capital that may be included in the Tier 2 capital shall be a maximum of fifty percent (50%) of total Tier 1 capital (net of deductions therefrom): *Provided furthermore*, That the total amount of upper and lower Tier 2 capital that may be included in the qualifying capital shall be a maximum of 100% of total Tier 1 capital (net of deductions therefrom);

c. *Less deductions from the total of Tier 1 and Tier 2 capital, as follows:*

(1) Investments in equity of unconsolidated subsidiary banks and other subsidiary financial allied undertakings, but excluding insurance companies (for solo basis);

(2) Investments in debt capital instruments of unconsolidated subsidiary banks (for solo basis);

(3) Investments in equity of subsidiary insurance companies and subsidiary non-financial allied undertakings;

(4) Reciprocal investments in equity of other banks/enterprises; and

(5) Reciprocal investments in unsecured subordinated term debt instruments of other banks/QBs in excess of the lower of (i) an aggregate ceiling of five percent (5%) of total Tier 1 capital of the QB; or (ii) ten percent (10%) of the total outstanding unsecured subordinated term debt issuance of the other bank/QB:

Provided, That any asset deducted from the qualifying capital in computing the numerator of the risk-based capital ratio shall not be included in the risk-weighted assets in computing the denominator of the ratio.

(As amended by Circular No. 560 dated 31 January 2007)

§ 4116Q.3 ***(2008 - 4116Q.2) Risk-weighted assets.*** The risk-weighted assets shall be determined by assigning risk weights to amounts of on-balance sheet assets and to credit equivalent amounts of off-balance sheet items (inclusive of derivative contracts): *Provided,* That the following shall be deducted from the total risk-weighted assets:

(1) general loan loss provision (in excess of the amount permitted to be included in UT2 capital); and

(2) unbooked valuation reserves and other capital adjustments affecting asset accounts based on the latest report of

examination as approved by the Monetary Board.

a. *On-balance sheet assets*. The risk-weighted amount shall be the product of the book value of the asset multiplied by the risk weight associated with that asset, as follows:

(1) *Zero percent (0%) risk weight*

(a) Cash on hand;

(b) Claims on or portions of claims guaranteed by or collateralized by securities issued by -

(i) Philippine national government and BSP; and

(ii) Central governments and central banks of foreign countries with the highest credit quality as defined in Subsec. 4116Q.4;

(c) Loans to the extent covered by hold-out on, or assignment of deposit substitutes maintained with the lending QB;

(d) Portions of loans covered by Industrial Guarantee and Loan Fund (IGLF) guarantee;

(e) Real estate mortgage (REM) loans to the extent guaranteed by the Home Guaranty Corporation (HGC);

(f) Loans to the extent guaranteed by the Trade and Investment Development Corporation of the Philippines (TIDCORP);

(g) Residual value of leased equipment to the extent covered by deposits on lease contracts (for FCs);

(h) Lease contract receivables to the extent covered by the excess of deposits on lease contracts over residual value of leased equipment (for FCs); and

(i) Foreign currency notes and coins on hand acceptable as international reserves;

(2) *Twenty percent (20%) risk weight*

(a) Checks and other cash items (COCIs);

(b) Claims on or portions of claims guaranteed by or collateralized by securities issued by non-central government public sector entities of foreign countries with the highest credit quality as defined in Subsec. 4116Q.4;

(c) Claims on or portions of claims guaranteed by Philippine incorporated banks/QBs with the highest credit quality as defined in Subsec. 4116Q.4;

(d) Claims on or portions of claims guaranteed by foreign incorporated banks with the highest credit quality as defined in Subsec. 4116Q.4;

(e) Claims on or portions of claims guaranteed by or collateralized by securities issued by multilateral development banks (MDBs);

(f) Loans to exporters to the extent guaranteed by Small Business Guarantee and Finance Corporation (SBGFC); and

(g) Foreign currency COCIs denominated in currencies acceptable as international reserves;

(3) *Fifty percent (50%) risk weight* -

(a) Loans for housing purpose, fully secured by first mortgage on residential property that is or will be occupied or leased out by the borrower; and

(b) Local government unit (LGU) bonds which are covered by deed of assignment of Internal Revenue Allotment (IRA) of the LGU and guaranteed by the LGU Guarantee Corporation;

(4) *One hundred percent (100%) risk weight* -

All other assets including, among others, the following:

(a) Claims on central governments and central banks of foreign countries other than those with the highest credit quality;

(b) Claims on Philippine (LGUs);

(c) Claims on non-central government public sector entities of foreign countries other than those with the highest credit quality;

(d) Claims on government-owned or controlled commercial corporations;

(e) Claims on Philippine incorporated banks/QBs other than those with the highest credit quality;

(f) Claims on foreign incorporated banks other than those with the highest credit quality;

(g) Loans to companies engaged in speculative residential building or property development;

(h) Claims on the private sector (except those deducted from capital);

(i) Equity investments (except those deducted from capital);

(j) Equipment and other real estate for lease (for FCs);

(k) Real estate for sale/lease;

(l) QB premises, furniture, fixtures and equipment (net);

(m) Appraisal increment - QB premises, furniture, fixtures and equipment (net);

(n) Real and other properties owned or acquired (net);

(o) Foreign currency notes and coins on hand not acceptable as international reserves; and

(p) Foreign COCIs not denominated in foreign currencies acceptable as international reserves, except those which are deducted from capital, as follows:

(i) Unsecured credit accommodations, both direct and indirect, to DOSRI;

(ii) Deferred income tax;

(iii) Goodwill;

(iv) Sinking fund for redemption of limited life redeemable preferred stock;

(v) Equity investments in unconsolidated subsidiary banks and other subsidiary financial allied undertakings, but excluding insurance companies;

(vi) Investments in debt capital instruments of unconsolidated subsidiary banks;

(vii) Equity investments in subsidiary insurance companies and subsidiary non-financial allied undertakings;

(viii) Reciprocal investments in equity of other banks/enterprises; and

(ix) Reciprocal investments in unsecured subordinated term debt instruments of other banks/QBs, in excess of the lower of (i) an aggregate ceiling of five percent (5%) of total Tier 1 capital of the QB; or (ii) ten percent (10%) of the total outstanding unsecured subordinated term debt issuance of the other bank/QB;

b. *Off-balance sheet items*. The risk-weighted amount shall be calculated using a two (2)-step process.

First, the credit equivalent amount of an off-balance sheet item shall be determined by multiplying its notional principal amount by the appropriate credit conversion factor, as follows:

(1) *One hundred percent (100%) credit conversion factor* -

This shall apply to direct credit substitutes, e.g. general guarantees of indebtedness and acceptances (including endorsements with the character of acceptances), and shall include -

(a) Outstanding guarantees issued

This shall also apply to sale and repo agreements and asset sales with recourse where the credit risk remains with the QB [to the extent not included in the (BS)], as well as to forward asset purchases, and partly-paid shares and securities, which represent commitments with certain drawdown: *Provided,* That these items shall be weighted according to the type of asset and not according to the type of counterparty with whom the transaction has been entered into.

(2) *Fifty percent (50%) credit conversion factor* - This shall apply to -

(a) Note issuance facilities and revolving underwriting facilities (for IHs); and

(b) Other commitments, e.g., formal standby facilities and credit lines with an original maturity of more than one (1) year. This shall include -

(i) Underwritten accounts unsold (for IHs).

(3) *Zero percent (0%) credit conversion factor* -

This shall apply to commitments with an original maturity of up to one (1) year.

This shall also apply to those not involving credit risk, and shall include -

(a) Items held for safekeeping/ custodianship;

(b) Trust department accounts;

(c) Items held as collaterals; etc.

Second, the credit equivalent amount shall be treated like any on-balance sheet asset and shall be assigned the appropriate risk weight, i.e., according to the obligor, or if relevant, the qualified guarantor or the nature of collateral.

c. *Derivative contracts*. The credit equivalent amount shall be the sum of the current credit exposure (or replacement cost) and an estimate of the potential future credit exposure (or add-on): *Provided*, That the following shall not be included in the computation:

(1) Instruments which are traded on exchange where they are subject to daily receipt and payment of cash variation margin; and

(2) Exchange rate contracts with original maturity of fourteen (14) calendar days or less.

The current credit exposure shall be the positive mark-to-market value of the contract (or zero if the mark-to-market value is zero or negative). The potential future credit exposure shall be the product of the notional principal amount of the contract multiplied by the appropriate potential future credit conversion factor, as indicated below:

Interest Residual Maturity	Exchange Rate Contract	Rate Contract
One (1) year or less	0.0%	1.0%
Over one (1) year to five (5) years	0.5%	5.0%
Over five (5) years	1.5%	7.5%

Provided, That for contracts with multiple exchanges of principal, the factors are to be multiplied by the number of remaining payments in the contract: *Provided, further,* That for contracts that are structured to settle outstanding exposure following specified payment dates and where the terms are reset such that the market value of the contract is zero on these specified dates, the residual maturity would be set equal to the time until the next reset date, and in the case of interest rate contracts with remaining maturities of more than one (1) year that meet these criteria, the potential future credit conversion factor is subject to a floor of five tenths percent (0.5%): *Provided, furthermore,* That no potential future credit exposure shall be calculated for single currency floating/ floating interest rate swaps, i.e., the credit exposure on these contracts would be evaluated solely on the basis of their mark-to-market value.

The credit equivalent amount shall be treated like any on-balance sheet asset, and shall be assigned the appropriate risk weight, i.e., according to the obligor, or if relevant, the qualified guarantor or the nature of collateral: *Provided*, That a fifty percent (50%) risk weight shall be applied in respect of obligors which would otherwise attract a 100% risk weight.

The extent to which a claim is guaranteed/collateralized shall be determined by the amount of guarantee coverage/current market value of securities pledged, in comparison with the book value of the on-balance sheet asset or the notional principal amount of the off-balance sheet exposure, except for derivative contracts for which determination is generally made in relation to credit equivalent amount.

§ 4116Q.4 ***(2008 - 4116Q.3) Definitions***

a. *Amount due from the BSP*. This refers to all deposits of the reporting QB with the BSP.

b. *Appraisal increment reserve*. This shall form part of capital only if authorized by the Monetary Board.

c. *QB premises, furniture, fixtures and equipment net of depreciation*. This refers to the cost of land and improvements used as the QB premises, and furniture, fixtures and equipment owned by the QB.

d. *Cash on hand*. This refers to total cash held by the QB consisting of both notes and coins in Philippine currency.

e. *Central government of a foreign country*. This refers to the central government which is regarded as such by a recognized banking supervisory authority in that country.

f. *Claims*. This refer to loans or debt obligations of the entity on whom the claim is held, and shall include, but shall not be limited to, the following accounts, inclusive of accumulated market gains/(losses) and accumulated bond discount/(premium amortization), and net of specific allowance for probable losses:

(1) Due from BSP;

(2) Due from other banks;

(3) Interbank loans receivable;

(4) Loans and discounts, including lease contract receivables, net of advance leasing income received and receivables financed for Financing Companies (FCs);

(5) Restructured loans;

(6) Trading account securities - loans;

(7) Underwriting accounts - debt securities (for IHs);

(8) Underwriting accounts - equity securities (for IHs);

(9) Trading account securities - debt securities;

(10) Trading account securities - equity securities (for IHs);

(11) Available for sale securities;

(12) Investments in bonds and other debt instruments (IBODI); and

(13) Others, e.g., accounts receivable and accrued interest receivable.

Accruals on a claim shall be classified and risk weighted in the same way as the claim.

g. *Consolidated basis*. This refers to combined statement of condition (SOC) of parent QB and subsidiary financial allied undertakings, but excluding insurance companies.

h. *Debt capital instruments*. This refers to unsecured subordinated term debt instruments qualifying as capital of banks.

i. *Equity investments*. This refers to investments in capital stock of companies, firms or enterprises, made for purposes of control, affiliation or other continuing business advantage.

j. *Exchange rate contracts*. This includes cross-currency interest rate swaps, forward foreign exchange (FX) contracts, currency futures, currency options purchased and similar instruments.

k. *Financial allied undertakings*. This refers to enterprises or firms with homogenous or similar activities/business/functions with the financial intermediary and may include but not limited to leasing companies, banks, IHs, FCs, credit card companies, FIs catering to small and medium scale industries (including venture capital corporations), companies engaged in stock brokerage/securities dealership, companies engaged in FX dealership/brokerage, holding companies, and such other similar activities as the Monetary Board may declare as appropriate from time to time, but excluding insurance companies.

l. *Foreign country/foreign incorporated bank and Philippine incorporated bank/QB with the highest credit quality*. This refers to a foreign country/foreign incorporated bank and Philippine incorporated bank/QB given the highest credit rating of any two (2) of the following internationally accepted rating agencies:

Rating Agency	Highest Rating
(1) Moody's	"Aa3" and above
(2) Standard and Poor's	"AA-" and above
(3) Fitch IBCA	"AA-" and above
(4) Others as may be approved by the Monetary Board	

m. *Forward asset purchases*. This refers to a commitment to purchase a loan, security or other asset at a specified future date, usually on pre-arranged terms.

n. *Goodwill*. This refers to an intangible asset that represents the excess of the purchase price over the fair market value of identifiable assets acquired less liabilities assumed in acquisitions accounted for under the purchase method of accounting.

o. *Interest rate contracts*. This includes single-currency interest rate swaps, basis swaps, forward rate agreements, interest rate futures, interest rate options purchased and similar instruments.

p. *Loans for housing purpose, fully secured by first mortgage on residential property that is or will be occupied or leased out by the borrower*. This shall not include loans to companies engaged in speculative residential building or property development.

q. *Loans to the extent covered by hold-out on, or assignment of deposit substitutes maintained in the lending QB*. A loan shall be considered as secured by a hold-out on, or assignment of deposit substitute only if such deposit substitute account is covered by a hold-out agreement or deed of assignment signed by the investor/placer in favor of the QB. This shall not include loans transferred to/carried by the QB's trust department secured by deposit substitute hold-out/assignment.

r. *MDBs*. This refers to International Bank for Reconstruction and Development (IBRD), Inter-American Development Bank, Asian Development Bank (ADB), African Development Bank (AfDB), European Investment Bank (EIB) and European Bank for Reconstruction and Development.

s. *Non-central government public sector entity of a foreign country*. This refers to entities which are regarded as such by a recognized banking supervisory authority in the country in which they are incorporated.

t. *Note issuance facilities and revolving underwriting facilities*. This refers to an arrangement whereby a borrower may draw down funds up to a prescribed limit over an extended period by repeated issues to the market of promissory notes which the QB committed to underwrite.

u. *Other commitments*. This includes undrawn portion of any binding arrangements which obligate the QB to provide funds at some future date.

v. *Other commitments with an original maturity of up to one (1) year*. This includes any revolving or undated open-ended commitments, e.g., unused credit lines: *Provided,* That these can be unconditionally cancelled at any time and are subject to credit revision at least annually.

w. *Partly-paid shares and securities*. This arises where only a part of the issue price or nominal face value of a security purchased has been subscribed and the issuer may call for the outstanding balance (or a further installment), either on a date predetermined at the time of issue, or at an unspecified future date.

x. *Perpetual preferred stock*. This refers to preferred stock that does not have a maturity date, that cannot be redeemed at the option of the holder of the instrument, and that has no provision that will require future redemption of the issue. Consistent with these provisions, any perpetual preferred stock with a feature permitting redemption at the option of the issuer may qualify as capital only if the redemption is subject to prior approval of the BSP.

y. *Philippine LGUs*. This refers to the Philippine government units below the level of national government, such as city, provincial, and municipal governments.

z. *Philippine national government*. This shall refer to the Philippine national government and its agencies such as departments, bureaus, offices, and instrumentalities, but excluding

government owned and-controlled commercial corporations.

(1) *Private sector*. This refers to entities other than banks, QBs and governments. This shall also include commercial companies owned by the public sector, such as government-owned or-controlled commercial corporations.

(2) *Redeemable preferred stock*. This refers to preferred stock which may be redeemed at the specific dates or periods fixed for redemption.

(3) *Sale and repo agreements and asset sales with recourse*. This refers to arrangements whereby a QB sells a loan, security or fixed asset to a third party with a commitment to repurchase the asset after a certain time, or in the event of a certain contingency.

(4) *Solo basis*. This refers to combined SOC of head office and branches.

(5) *Subsidiary*. This refers to a corporation or firm more than fifty percent (50%) of the outstanding voting stock of which is directly or indirectly owned, controlled or held with the power to vote by a QB.

(6) *Treasury shares*. This refers to the QB's own shares of stock that have been issued and fully paid for, subsequently reacquired through purchase or donations and have not been cancelled or re-issued. This also refers to shares of a parent QB held by a subsidiary financial allied undertaking in a consolidated statement of condition (CSOC).

§ 4116Q.5 ***(2008 - 4116Q.4) Required reports.*** QBs shall submit a report of their risk-based CAR on a solo basis (head office plus branches) and on a consolidated basis (parent QB plus subsidiary financial allied undertakings, but excluding insurance companies) quarterly to the appropriate department of the SES in the prescribed forms within the deadlines, i.e., fifteen (15) business days and thirty (30) business days after the end of reference quarter, respectively. Only QBs with subsidiary financial allied undertakings (excluding insurance companies) which under existing regulations are required to prepare consolidated statements of condition on a line-by-line basis shall be required to submit report on consolidated basis. The above-mentioned reports shall be classified as *Category A-2* reports.

§ 4116Q.6 ***(2008 - 4116Q.5) Sanctions*** Whenever the capital accounts of a QB are deficient with respect to the prescribed CAR, the Monetary Board after considering a report of the appropriate department of the SES on the state of solvency of the institution concerned, shall limit or prohibit the distribution of the net profits and shall require that part or all of net profits be used to increase the capital accounts of the QB until the minimum requirement has been met. The Monetary Board may restrict or prohibit the making of new investments of any sort by the QB, with the exception of purchases of readily marketable evidences of indebtedness issued by the Philippine national government and BSP included in Item *"a(1)(b)i"* of Subsec. 4116Q.3, until the minimum required capital ratio has been restored.

§ 4116Q.7 ***(2008 - 4116Q.6) Temporary relief.*** In case of QB merger or consolidation, or when a QB is under rehabilitation under a program approved by the BSP, the Monetary Board may temporarily relieve the surviving QB, consolidated QB, or constituent QB or corporations under rehabilitation from full compliance with the required capital ratio for a maximum period of one (1) year.

Sec. 4117Q Treatment of Equity Investment with Reciprocal Stockholdings. For purposes of computing the prescribed ratio of net worth (or combined capital accounts)

to risk assets, equity investments of a QB in another QB shall be deducted from its net worth if the investee QB has a reciprocal equity investment in the investing QB, in which case the investment of the QB or the reciprocal investment of the other QB, whichever is lower, shall be deducted from the net worth of the QBs.

Sec. 4118Q Sanctions on Net Worth Deficiency

a. Any QB which is deficient in the capital requirement under Sec. 4115Q shall be liable to the following sanctions:

(1) In case of capital deficiency for five (5) or more times within a reporting period:

(a) For the first offense - a fine of P3,000.

(b) For the second consecutive offense - prohibition from extending new loans or making new investments for a period of thirty (30) calendar days.

New loans and new investments shall refer to any loan or investment involving disbursement of funds, except GS.

(c) For the third consecutive offense - extension of the penalty under the preceding paragraph for another thirty (30) calendar days.

(d) For the fourth consecutive offense - suspension of the Certificate of Authority to engage in quasi-banking functions for a period of thirty (30) calendar days. The suspension shall be automatically lifted if in the final reporting period of the period of suspension, the entity maintains the minimum capital required under Sec. 4115Q and 4116Q as may be applicable for every day of such reporting period.

(2) In case of continuous capital deficiency:

(a) For two (2) consecutive reporting periods - suspension of the Certificate of Authority to engage in quasi-banking functions for a period of thirty (30) calendar days.

(b) For every consecutive reporting period, the suspension shall extend for another thirty (30) calendar days.

(c) The suspension shall be automatically lifted if on the final reporting period of the period of suspension, the entity maintains the minimum capital required under Secs. 4115Q and 4116Q as may be apllicable for every day of such reporting period.

(3) In all of the cases abovementioned, establishment of branches, agencies, extension offices, etc., shall be suspended.

b. For improperly accomplished report, QBs shall pay P600 per day for every day the report is not corrected, counted as of the date the error is brought to its attention until the corrected report is submitted.

c. For willfully making false statements in the report or submitting a false report, the Certificate of Authority for quasi-banking functions shall be suspended/revoked.

d. The Monetary Board may impose additional sanctions on the entity engaged in quasi-banking functions by:

(1) Revoking the Certificate of Authority to engage in quasi-banking functions; and

(2) Such other sanctions as the BSP may deem necessary.

(As amended by Circular No. 585 dated 15 October 2007)

Sec. 4119Q Internal Capital Adequacy Assessment Process and Supervisory Review Process. The guidelines on internal capital adequacy assessment process (ICAAP) and BSP's supervisory review process (SRP) are shown in *Appendices Q-53 and Q-54 respectively*.

The ICAAP guidelines shall apply to all UBs and KBs on a group-wide basis.

All covered UBs and KBs are required to submit the interim ICAAP document on or before 30 April 2010 and the final ICAAP document together with the Corporate Secretary's Certificate attesting to the approval by the bank's board of directors on or before 31 January 2011.

The guidelines shall take effect on 01 January 2011.

(Circular No. 639 dated 15 January 2009, as amended by Circular No. 29 December 2009)

Sec. 4120Q (Reserved)

F. (RESERVED)

Secs. 4121Q - 4135Q (Reserved)

G. STOCK, STOCKHOLDERS AND DIVIDENDS

Sec. 4136Q *(2008 - 4126Q)* Dividends Pursuant to Section 57 of R.A. No. 8791, no QB shall declare dividends greater than its accumulated net profits then on hand, deducting therefrom its losses and bad debts. Neither shall the QB declare dividends if, at the time of declaration, it has not complied with the provisions of Subsec. 4136Q.2.

§ 4136Q.1 *(2008 - 4126Q.1) Definition of terms.* For purposes of this Section, the following definitions shall apply:

a. *Bad debts* shall include any debt on which interest is past due for a period of six (6) months, unless it is well secured and in process of collection.

A loan payable in installment with an automatic acceleration clause shall be considered a bad debt within the contemplation of this Section where installments or amortizations have become past due for a period of six (6) months, unless the loan is well secured and in process of collection. For a loan payable in installments without an acceleration clause, only the installments or amortizations that have become past due for a period of six (6) months and which are not well secured and in the process of collection shall be considered bad debts within the contemplation of this Section.

b. *Well secured* - A debt shall be considered well secured (or fully secured) if it is covered by collateral in the form of a duly constituted mortgage, pledge, or lien on real or personal properties, including securities. The outstanding debt, accrued interest and other pertinent fees and expenses thereon shall not be in excess of seventy percent (70%) of the appraised value (AV) of real estate, or fifty percent (50%) of the other personal properties offered as lien.

c. *In process of collection* - A debt due to a QB shall be considered in process of collection when it is the subject of continuing extrajudicial or judicial proceedings aimed towards its full settlement or liquidation, or otherwise to place it in current status.

The extrajudicial proceedings, such as the writing of collection or demand letters, must have been initiated by the QB and/or its lawyers before the interest or installments or amortizations on the debt become past due and unpaid for a period of six (6) months.

The debt shall continue to be considered in process of collection for a period of six (6) months counted from date of the first collection or demand letter and if, within this period, the debtor fails to make a payment of at least twenty percent (20%) of the outstanding balance of the principal on his account, plus all interests which may have accrued thereon, the same shall automatically be classified as bad debt unless judicial proceedings are instituted.

The debt shall continue to be considered in process of collection during the pendency of the judicial proceedings. When judgment against the debtor has been obtained, the QB must be active in enforcing the judgment for the debt to continue to be considered in process of collection.

§ 4136Q.2 *(2008 - 4126Q.2) Requirements on the declaration of dividends/net amount available for dividends*

a. *Requirements on the declaration of dividends*. At the time of declaration, QBs shall have complied with the following:

(1) Clearing account with the BSP is not overdrawn;

(2) Minimum capitalization requirement and risk-based capital ratio;

(3) Statutory and liquidity reserves requirement;

(4) No past due loans with any institution;

(5) No net losses from operations in any one of the two (2) fiscal years immediately preceding the date of dividend declaration; and

(6) Has not committed any of the following major violations:

(a) Loans and other credit accommodations and guarantees granted in excess of the single borrower's limit;

(b) Loans and other credit accommodations granted/extended in excess of the ceilings on accommodations to DOSRI;

(c) Unsafe and unsound banking practice as defined under existing BSP regulations;

(d) Equity investments in excess of the prescribed ceilings;

(e) Investments in real estate, QB premises and equipment in excess of prescribed ceilings;

(f) Major violations/exceptions cited in the previous examination not duly acted upon or not yet corrected;

(g) Transactions or activities without prior approval or necessary license from the BSP such as, but not limited to derivatives, trust and e-banking;

(h) Refusal to permit examination into the affairs of the institution or any willful making of a false or misleading statement to the Monetary Board or to the appropriate department of the SES; and

(i) Failure to comply with the capital build-up program approved by the Monetary Board.

QBs which have committed any of the major violations under Item *"a(6)"* above may only be allowed to declare dividends by the Monetary Board upon recommendation of the appropriate department of the SES that the QB has corrected the major violation/s that it has committed.

b. *Amount available*. The net amount available for dividends shall be the amount of unrestricted or free retained earnings and profit and loss summary less:

(1) Bad debts against which valuation reserves are not required by the BSP to be set up;

(2) Unbooked valuation reserves, and other unbooked capital adjustments required by the BSP, whether or not allowed to be set up on a staggered basis;

(3) Deferred income tax;

(4) Accumulated profits not yet received but already recorded by the QB representing its share in profits of its subsidiaries under the equity method of accounting;

(5) Accrued interest as required to be excluded pursuant to Item *"c"* of Subsec. 4305Q.4, net of booked valuation reserves on accrued interest receivable or allowance for uncollectible interest on loans; and

(6) FX profit arising from revaluation of FX denominated accounts.

(As amended by Circular No. 571 dated 21 June 2007)

§ 4136Q.3 *(Reserved)*

§ 4136Q.4 *(2008 - 4126Q.3) Reporting and verification.* Declaration of cash dividend shall be reported by the QB concerned to the appropriate department of the SES within ten (10) business days from date of approval of the declaration by the QB's board of directors, in the prescribed form.

Pending verification of abovementioned report by the appropriate department of the SES, the QB concerned shall not make any announcement or communication on the declaration of cash dividends nor shall any payment be made thereon.

In any case, the declaration may be announced and the dividends paid, if, after thirty (30) business days from the date the report required herein shall have been received by the BSP, no advice against such declaration has been received by the QB concerned, subject to the condition that the record date for such dividends cannot be set earlier than thirty (30) business days after declaration.

QBs whose shares are listed with any domestic stock exchange may give notice of cash dividend declaration in accordance with pertinent rules of the SEC: *Provided,* That no record date is fixed for such cash dividend, pending verification of the report

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on such declaration by the appropriate department of the SES.

§ 4136Q.5 ***(2008 - 4126Q.4) Recording of dividends.*** The liability for cash dividends declared shall be taken up in the books upon receipt of BSP approval thereof, or if no such approval is received, after thirty (30) business days from the date required report on cash dividend declaration was received by the appropriate department of the SES, whichever comes earlier. A memorandum entry may be made to record the dividend declaration on the date of approval by the board of directors and for full disclosure purposes. The cash dividends may be disclosed in the financial statements by means of a footnote which should include a statement to the effect that the dividend declaration is subject to review by the BSP. Dividends of all kinds, whether on common or on preferred shares of stock, shall not be treated as interest expense, considering that as a general policy only irredeemable stock may be issued by QBs.

§ 4136Q.6 ***(Reserved)***

§ 4136Q.7 ***(2008 - 4126Q.5) Rules on declaration of stock dividends.*** The declaration of stock dividends shall be subject to the preceding regulations on declaration of cash dividends. Additional paid-in capital may be included in the amount available for stock dividends.

Secs. 4137Q - 4140Q (Reserved)

H. DIRECTORS, OFFICERS AND EMPLOYEES

Sec. 4141Q Definition; Qualifications; Powers; Responsibilities and Duties of Board of Directors and Directors. The following shall be the definition, qualifications, powers, responsibilities and duties of the board of directors and directors.

§ 4141Q.1 ***Limits on the number of the members of the board of directors*** Pursuant to Sections 15 and 17 of R.A. No. 8791, there shall be at least five (5), and a maximum of fifteen (15) members of the board of directors of a QB/trust entity two (2) of whom shall be independent directors: *Provided,* That in case of a QB/trust entity merger or consolidation, the number of directors may be increased up to twenty-one (21).

An *independent director* shall mean a person who -

(1) Is not or has not been an officer or employee of the QB/trust entity, its subsidiaries or affiliates or related interests during the past three (3) years counted from the date of his election;

(2) Is not a director or officer of the related companies of the institution's majority stockholder;

(3) Is not a majority stockholder of the institution, any of its related companies, or of its majority shareholders;

(4) Is not a relative within the fourth degree of consanguinity or affinity, legitimate or common-law of any director, officer or majority shareholder of the QB/trust entity or any of its related companies;

(5) Is not acting as a nominee or representative of any director or substantial shareholder of the QB/trust entity, any of its related companies or any of its substantial shareholders; and

(6) Is not retained as professional adviser, consultant, agent or counsel of the institution, any of its related companies or any of its substantial shareholders, either in his personal capacity or through his firm; is independent of management and free from any business or other relationship, has not engaged and does not engage in any transaction with the institution or with any of its related companies or with any of its substantial shareholders, whether by himself or with other persons or through a firm of which he is a partner or a company

of which he is a director or substantial shareholder, other than transactions which are conducted at arms length and could not materially interfere with or influence the exercise of his judgment.

An independent director of a QB/trust entity can be elected as an independent director of its: (a) parent or holding company; (b) subsidiary or affiliate; (c) substantial shareholder; or (d) other related companies, or vice-versa: *Provided,* That he is not a substantial shareholder of the QB/trust entity or any of the said concerned entities.

The terms and phrases used in *Items "(1)"* to *"(6)"* shall have the following meaning:

(a) *Parent* is a corporation which has control over another corporation directly or indirectly through one (1) or more intermediaries.

(b) *Subsidiary* means a corporation more than fifty percent (50%) of the voting stock of which is owned or controlled directly or indirectly through one (1) or more intermediaries by a QB/trust entity.

(c) *Affiliate* is a juridical person that directly or indirectly, through one (1) or more intermediaries, is controlled by, or is under common control with the QB/trust entity or its affiliates.

(d) *Related interests* as defined under Sections 12 and 13 of R.A. No. 8791 shall mean individuals related to each other within the fourth degree of consanguinity or affinity, legitimate or common law, and two (2) or more corporations owned or controlled by a single individual or by the same family group or the same group of persons.

(e) *Control* exists when the parent owns directly or indirectly through subsidiaries more than one-half of the voting power of an enterprise unless, in exceptional circumstance, it can be clearly demonstrated that such ownership does not constitute control. Control may also exist even when ownership is one-half or less of the voting power of an enterprise when there is:

(i) power over more than one-half of the voting rights by virtue of an agreement with other stockholders; or

(ii) power to govern the financial and operating policies of the enterprise under a statute or an agreement; or

(iii) power to appoint or remove the majority of the members of the board of directors or equivalent governing body; or

(iv) power to cast the majority votes at meetings of the board of directors or equivalent governing body; or

(v) any other arrangement similar to any of the above.

(f) *Related company* means another company which is: (a) its parent or holding company; (b) its subsidiary or affiliate; or (c) a corporation where a QB/trust entity or its majority stockholder own such number of shares that will allow/enable him to elect at least one (1) member of the board of directors or a partnership where such majority stockholder is a partner.

(g) *Substantial or major shareholder* shall mean a person, whether natural or juridical, owning such number of shares that will allow him to elect at least one (1) member of the board of directors of a QB/trust entity or who is directly or indirectly the registered or beneficial owner of more than ten percent (10%) of any class of its equity security.

(h) *Majority stockholder or majority shareholder* means a person, whether natural or juridical, owning more than fifty percent (50%) of the voting stock of a QB/trust entity.

Non-Filipino citizens may become members of the board of directors of a QB/trust entity to the extent of the foreign participation in the equity of said QB/trust entity: *Provided,* That pursuant to Section 23 of the Corporation Code of the Philippines (BP Blg. 68), a majority of the

directors must be residents of the Philippines.

The meetings of the board of directors may be conducted through modern technologies such as, but not limited to, teleconferencing and videoconferencing as long as the director who is taking part in said meetings can actively participate in the deliberations on matters taken up therein: *Provided*, That every member of the board shall participate in at least fifty percent (50%) and shall physically attend at least twenty-five percent (25%) of all board meetings every year: *Provided, further,* That in the case of a director who is unable to physically attend or participate in board meetings via teleconferencing or videoconferencing, the corporate secretary shall execute a notarized certification attesting that said director was given the agenda materials prior to the meeting and that his/her comments/ decisions thereon were submitted for deliberation/discussion and were taken up in the actual board meeting, and that the submission of said certification shall be considered compliance with the required fifty percent (50%) minimum attendance in board meetings.

§ 4141Q.2 *Qualifications of a director*

A director shall have the following minimum qualifications:

a. He shall be at least twenty-five (25) years of age at the time of his election or appointment;

b. He shall be at least a college graduate or have at least five (5) years experience in business;

c. He must have attended a special seminar for board of directors conducted or accredited by the BSP: *Provided*, That incumbent directors as well as those elected after 17 September 2001 must attend said seminar on or before 31 December 2002 or within a period of six (6) months from date of election for those elected after 31 December 2002, as the case may be; and

d. He must be fit and proper for the position of a director of the QB/trust entity. In determining whether a person is fit and proper for the position of a director, the following matters must be considered: integrity/probity, competence, education, diligence and experience/training.

The foregoing qualifications for directors shall be in addition to those required or prescribed under R.A. No. 8791 and other existing applicable laws and regulations.

§ 4141Q.3 *Powers/responsibilities and duties of board of directors and directors*

a. *Powers of the board of directors.* The corporate powers of a QB/trust entity shall be exercised, its business conducted and all its property shall be controlled and held by its board of directors. The powers of the board of directors as conferred by law are original and cannot be revoked by the stockholders. The directors hold their office charged with the duty to act for the QB/trust entity in accordance with their best judgment.

b. *General responsibility of the board of directors*. The position of a QB/trust entity director is a position of trust. A director assumes certain responsibilities to different constituencies or stakeholders, i.e., the QB/trust entity itself, its stockholders, its clients and other creditors, its management and employees, and the public at large. These constituencies or stakeholders have the right to expect that the institution is being run in a prudent and sound manner.

The board of directors is primarily responsible for the corporate governance of the QB/trust entity. To ensure good governance of the QB/trust entity, the board of directors should establish strategic objectives, policies and procedures that will guide and direct the activities of the

QB/trust entity and the means to attain the same as well as the mechanism for monitoring management's performance. While the management of the day-to-day affairs of the institution is the responsibility of the management team, the board of directors is, however, responsible for monitoring and overseeing management action.

c. Specific duties and responsibilities of the board of directors

(1) To select and appoint officers who are qualified to administer the QB's/trust entity's affairs effectively and soundly and to establish adequate selection process for all personnel. It is the primary responsibility of the board of directors to appoint competent management team at all times. The board of directors should apply fit and proper standards on key personnel. Integrity, technical expertise and experience in the institution's business, either current or planned, should be the key considerations in the selection process. And because mutual trust and a close working relationship are important, the board's choice should share its general operating philosophy and vision for the institution. The board of directors shall establish an appropriate compensation package for all personnel which shall be consistent with the interest of all stakeholders.

(2) *To establish objectives and draw up a business strategy for achieving them*. Consistent with the institution's objectives, business plans should be established to direct its on-going activities. The board should ensure that performance against plan is regularly reviewed, with corrective action taken as needed.

(3) *To conduct the affairs of the institution with high degree of integrity*. Since reputation is a very valuable asset, it is in the institution's best interest that in dealings with the public, it observes a high standard of integrity. The board of directors should prescribe corporate values, codes of conduct and other standards of appropriate behaviour for itself, the senior management and other employees. Among others, activities and transactions that could result or potentially result in conflict of interest, personal gain at the expense of the institution, or unethical conduct shall be strictly prohibited. It should provide policies that will prevent the use of the facilities of the QB/trust entity in furtherance of criminal and other illegal activities.

(4) *To establish and ensure compliance with sound written policies*. The board should adopt written policies on all major business activities, i.e., investments, loans, asset and liability management, business planning and budgeting. A mechanism to ensure compliance with said policies shall also be provided.

(5) *To prescribe a clear assignment of responsibilities and decision-making authorities, incorporating a hierarchy of required approvals from individuals to the board of directors*. The board should establish in writing the limits of the discretionary powers of each officer, committee, sub-committee and such other group for the purpose of lending, investing or committing the QB/trust entity to any financial undertaking or exposure to risk at any time. The board should have a schedule of matters and authorities reserved to it for decision, such as: major capital expenditures, equity investments and divestments.

(6) *To effectively supervise the QB's/trust entity's affairs*. As QBs/trust entities are entrusted with the handling and investment of public funds, the supervision required from the board involves a higher degree of wisdom, prudence, good business judgment and competence than that of directors of ordinary companies. Although directors may delegate certain authority to senior officers, it is their responsibility to supervise and be

responsible for the institution's sound management, as well as its problems. The board of directors should establish a system of checks and balances which applies in the first instance to the board itself. Among the members of the board, an effective system of checks and balances must exist. The system should also provide a mechanism for effective check and control by the board over the chief executive officer (CEO) and key managers and by the latter over the line officers of the QB/trust entity.

(7) *To monitor, assess and control the performance of management*. The board shall put in place an appropriate reporting system so that it is provided with relevant and timely information to be able to effectively assess the performance of management. For this purpose, it may constitute a governance committee.

(8) *To adopt and maintain adequate risk management policy*. The board of directors shall be responsible for the formulation and maintenance of written policies and procedures relating to the management of risks throughout the institution. The risk management policy shall include:

(a) a comprehensive risk management approach;

(b) a detailed structure of limits, guidelines and other parameters used to govern risk-taking;

(c) a clear delineation of lines of responsibilities for managing risk;

(d) an adequate system for measuring risk; and

(e) effective internal controls and a comprehensive risk-reporting process.

The board may constitute a committee for this purpose.

(9) *To constitute the following committees:*[1]

(a) Audit committee. The audit committee shall be composed of members of the board of directors, at least two (2) of whom shall be independent directors, including the chairman, preferably with accounting, auditing, or related financial management expertise or experience. The audit committee provides oversight of the institution's financial reporting and control and internal and external audit functions. It shall be responsible for the setting up of the internal audit department and for the appointment of the internal auditor as well as the independent external auditor who shall both report directly to the audit committee. It shall monitor and evaluate the adequacy and effectiveness of the internal control system.

Upon setting up the audit committee, the board of directors shall draw up a written charter or terms of reference which clearly sets out the audit committee's authority and duties, as well as the reporting relationship with the board of directors. This charter shall be approved by the board of directors and reviewed and updated periodically.

The audit committee shall have explicit authority to investigate any matter within its terms of reference, full access to and cooperation by management and full discretion to invite any director or executive officer to attend its meetings, and adequate resources to enable it to effectively discharge its functions.

The audit committee shall ensure that a review of the effectiveness of the institution's internal controls, including financial, operational and compliance controls, and risk management, is conducted at least annually.

The Audit Committee shall establish and maintain mechanisms by which officers and staff may, in confidence, raise concerns about possible improprieties or malpractices in matters of financial reporting, internal control, auditing or other issues to persons or entities that have the power to take corrective action. It shall ensure that arrangements are in place for

[1] Effective 01 January 2005 under Circular 456 dated 04 October 2004.

the independent investigation, appropriate follow-up action, and subsequent resolution of complaints.

(b) Corporate governance committee. The corporate governance committee shall assist the board of directors in fulfilling its corporate governance responsibilities. It shall review and evaluate the qualifications of all persons nominated to the board as well as those nominated to other positions requiring appointment by the board of directors. The committee shall be composed of at least three (3) members of the board of directors, two (2) of whom shall be independent directors.

The corporate governance committee shall have a written charter that describes the duties and responsibilities of its members. This charter shall be approved by the board of directors and reviewed and updated at least annually.

The committee shall be responsible for ensuring the board's effectiveness and due observance of corporate governance principles and guidelines. It shall oversee the periodic performance evaluation of the board and its committees and executive management; and shall also conduct an annual self-evaluation of its performance. The committee shall also decide whether or not a director is able to and has been adequately carrying out his/her duties as director bearing in mind the director's contribution and performance (e.g., competence, candor, attendance, preparedness and participation). Internal guidelines shall be adopted that address the competing time commitments that are faced when directors serve on multiple boards.

The committee shall make recommendations to the board regarding the continuing education of directors, assignment to board committees, succession plan for the board members and senior officers, and their remuneration commensurate with corporate and individual performance.

The corporate governance committee shall decide the manner by which the board's performance may be evaluated and propose an objective performance criteria approved by the board. Such performance indicators shall address how the board has enhanced long term shareholders' value.

(c) Risk management committee. The risk management committee shall be responsible for the development and oversight of the institution's risk management program. The committee shall be composed of at least three (3) members of the board of directors who shall possess a range of expertise as well as adequate knowledge of the institution's risk exposures to be able to develop appropriate strategies for preventing losses and minimizing the impact of losses when they occur. It shall oversee the system of limits to discretionary authority that the board delegates to management, ensure that the system remains effective, that the limits are observed and that immediate corrective actions are taken whenever limits are breached.

The risk management committee shall have a written charter that defines the duties and responsibilities of its members. The charter shall be approved by the board of directors and reviewed and refined periodically.

The core responsibility of the risk management committee are:

(i) *Identify and evaluate exposures*. The committee shall assess the probability of each risk becoming reality and shall estimate its possible effect and cost. Priority areas of concern are those risks that are the most likely to occur and are costly when they happen.

(ii) *Develop risk management strategies*. The risk management committee shall develop a written plan defining the strategies for managing and controlling the major risks. It shall identify

practical strategies to reduce the chance of harm and failure or minimize losses if the risk becomes real.

(iii) *Implement the risk management plan*. The risk management committee shall communicate the risk management plan and loss control procedures to affected parties. The committee shall conduct regular discussions on the institution's current risk exposure based on regular management reports and direct concerned units or offices on how to reduce these risks.

(iv) *Review and revise the plan as needed*. The committee shall evaluate the risk management plan to ensure its continued relevancy, comprehensiveness, and effectiveness. It shall revisit strategies, look for emerging or changing exposures, and stay abreast of developments that affect the likelihood of harm or loss. The committee shall report regularly to the board of directors the entity's over-all risk exposure, actions taken to reduce the risks, and recommend further action or plans as necessary.

(10) *To meet regularly*. To properly discharge its function, the board of directors shall meet regularly. Independent views in board meetings shall be given full consideration and all such meetings shall be duly minuted.

The meetings of the board of directors may be conducted through modern technologies such as, but not limited to, teleconferencing and video-conferencing as long as the director who is taking part in said meetings can actively participate in the deliberations on matters taken up therein: *Provided*, That every member of the board shall be physically present in at least fifty percent (50%) of all board meetings in every year.

(11) *To keep the individual members of the board and the shareholders informed*. It is the duty of the board to present to all its members and to the shareholders a balanced and understandable assessment of the QB's/ trust entity's performance and financial condition. It should also provide appropriate information that flows internally and to the public. All members of the board shall have reasonable access to any information about the institution.

(12) *To ensure that the QB/trust entity has beneficial influence on the economy*. The board has a continuing responsibility to provide those services and facilities which will be supportive of the national economy.

(13) *To assess at least annually its performance and effectiveness as a body, as well as its various committees, the CEO and the QB/trust entity itself*. The composition of the board shall also be reviewed regularly with the end in view of having a balanced membership. Towards this end, a system and procedure for evaluation shall be adopted which may include, but not limited to, the setting of benchmark and peer group analysis.

(14) *To keep their authority within the powers of the institution as prescribed in the articles of incorporation, charter, by-laws and in existing laws, rules and regulations*. To conduct and maintain the affairs of the institution within the scope of its authority as prescribed in its charter and in existing laws, rules and regulations, the board shall appoint a compliance officer who shall be responsible for coordinating, monitoring and facilitating compliance with existing laws, rules and regulations. The compliance officer shall be vested with appropriate authority and provided with appropriate support and resources. It may also constitute a compliance committee.

If the directors carry the institution into a transaction outside the scope of the business agreed upon in the articles, with resulting loss to the institution, they may be called upon to reimburse the institution for that loss. If directors willfully do an act, which they know or ought to know to be unauthorized, they are clearly liable to the institution for resulting damages.

d. *Specific duties and responsibilities of a director*

(1) *To conduct fair business transactions with the QB/trust entity and to ensure that personal interest does not bias board decisions*. A director should, whenever possible, avoid situations that would give rise to a conflict of interest. If transactions with the institution cannot be avoided, it should be done in the regular course of business and upon terms not less favorable to the institution than those offered to others. The basic principle to be observed is that a director should not use his position to make profit or to acquire benefit or advantage for himself and/or his related interests. He should avoid situations that would compromise his impartiality.

(2) *To act honestly and in good faith, with loyalty and in the best interest of the institution, its stockholders, regardless of the amount of their stockholdings, and other stakeholders such as its investors, borrowers, other clients and the general public*. A director must always act in good faith, with the care which an ordinarily prudent man would exercise under similar circumstances. While a director should always strive to promote the interest of all stockholders, he should also give due regard to the rights and interests of other stakeholders.

(3) *To devote time and attention necessary to properly discharge his duties and responsibilities*. A director should devote sufficient time to familiarize himself with the institution's business. He must be constantly aware of the institution's condition and be knowledgeable enough to contribute meaningfully to the board's work. He must attend and actively participate in board and committee meetings, request and review meeting materials, ask questions, and request explanations and be familiar with audits and supervisory communications. If a person cannot give sufficient time and attention to the affairs of the institution, he should neither accept his nomination nor run for election as member of the board.

(4) *To act judiciously*. Before deciding on any matter brought before the board of directors, every director should thoroughly evaluate the issues, ask questions and seek clarifications when necessary.

(5) *To exercise independent judgment*. A director should view each problem/situation objectively. When a disagreement with others occurs, he should carefully evaluate the situation and state his position. He should not be afraid to take a position even though it might be unpopular. Corollarily, he should support plans and ideas that he thinks will be beneficial to the institution.

(6) *To be generally informed of both the QB's/trust entity's business environment and legal and regulatory framework controlling its activities*. A director should have a working knowledge of the statutory and regulatory requirements affecting the institution, including the content of its articles of incorporation and by-laws, the requirements of the BSP and where applicable, the requirements of other regulatory agencies and must exercise care to see that these are not violated. He should also keep himself informed of the industry developments and business trends in order to safeguard the institution's competitiveness.

(7) *To observe confidentiality*. A director must observe the confidentiality of non-public information acquired by reason of his position as director. He may not disclose said information to any other person without the authority of the board.

§ 4141Q.4 *Confirmation of the election/appointment of directors and officers.* The election/appointment of directors and officers of QBs/trust entities shall be subject to confirmation by the:

Confirming Authority	Position Level
a. Monetary Board	director, president, chief executive officer, chief operating officer, senior vice president or equivalent rank of QBs/ trust entities with total assets of at least ₱1 billion.
b. A Committee to be composed of: • The Deputy Governor - SES • Managing Directors of SE I and II • Directors of the concerned appropriate department of the SES	director/trustee, senior vice president and above or equivalent rank of QBs/trust entities whose election/ appointment is not subject to confirmation by the Monetary Board

The election/appointment of all incumbent directors/trustees and officers of QBs/trust entities as of 17 September 2001 not previously approved/confirmed by the Monetary Board shall be submitted to the BSP through the appropriate department of the SES for confirmation.

§§ 4141Q.5 - 4141Q.8 *(Reserved)*

§ 4141Q.9 *Reports required.* QBs/ trust entities shall furnish all of their directors/ trustees with a copy of the specific duties and responsibilities of the board of directors/ trustees prescribed under Items *"b"* and *"c"* of Subsec. 4141Q.3 within thirty (30) business days from 17 May 2001 in cases of incumbent directors/trustees and at the time of election in cases of directors/trustees elected after such date.

The directors/trustees concerned shall each be required to acknowledge receipt of the copies of such specific duties and responsibilities and shall certify that they fully understand the same.

Copies of the acknowledgment and certification herein required shall be submitted in accordance with *Appendix Q-3*.

§ 4141Q.10 *Sanctions.* Without prejudice to the other sanctions prescribed under Section 37 of R.A. No. 7653 and to the provisions of Section 16 of R.A. No. 8791, any director/trustee of a QB/trust entity who violates or fails to observe and/ or perform any of the above responsibilities and duties shall for each violation or offense, be penalized for P15,000.

Sec. 4142Q Definition and Qualifications of Officers. *Officers* shall include the president, executive vice president (EVP), senior vice-president, vice president, general manager, treasurer, secretary, trust officer and others mentioned as officers of the QB/trust entity, or those whose duties as such are defined in the by-laws, or are generally known to be the officers of the QB/trust entity (or any of its branches and offices other than the head office) either through announcement, representation, publication or any kind of communication made by the QB/trust entity: *Provided*, That a person holding the position of chairman or vice-chairman of the board or another position in the board shall not be considered as an officer unless the duties of his position in the board include functions of management such as those ordinarily performed by regular officers: *Provided, further,* That members of a group or committee, including sub-groups or sub-committees, whose duties include functions of management such as those ordinarily performed by regular officers, and are not purely recommendatory or advisory, shall likewise be considered as officers.

An officer shall have the following minimum qualifications:

a. He shall be at least twenty-one (21) years of age;

b. He shall be at least a college graduate, or have at least five (5) years creditable experience or training in financial management or related activities, or in a field related to his position and responsibilities: *Provided, however,* That trust officers shall have at least five (5) years of actual experience in trust operations, or at least three (3) years of actual experience in trust operations and completed at least one (1) year training program in trust operations acceptable to the BSP, or at least five (5) years of actual experience as officer of a bank, NBFI or related activities and completed at least one (1) year training program in trust operations acceptable to the BSP; and

c. He must be fit and proper for the position he is being proposed/appointed to. In determining whether a person is fit and proper for a particular position, the following matters must be considered: integrity probity, competence, education, diligence and experience/training.

The foregoing qualifications for officers shall be in addition to those required or prescribed under R.A. No. 8791 and other existing applicable laws and regulations.

(As amended by Circular Nos. 665 dated 04 September 2009 and 562 dated 13 March 2007)

Sec. 4143Q Disqualification of Directors/ Trustees and Officers. The following regulations shall govern the disqualification of QB/trust entity directors/trustees and officers.

§ 4143Q.1 ***Persons disqualified to become directors/trustees.*** Without prejudice to specific provisions of law prescribing disqualifications for directors/ trustees, the following are disqualified from becoming directors/trustees:

a. *Permanently disqualified*

Directors/trustees/officers/ employees permanently disqualified by the Monetary Board from holding a director/trustee position:

(1) Persons who have been convicted by final judgment of a court for offenses involving dishonesty or breach of trust such as but not limited to, estafa, embezzlement, extortion, forgery, malversation, swindling, theft, robbery, falsification, bribery, violation of B.P. Blg. 22, violation of Anti-Graft and Corrupt Practices Act and prohibited acts and transactions under Section 7 of R.A. No. 6713 (Code of Conduct and Ethical Standards for Public Officials and Employees);

(2) Persons who have been convicted by final judgment of a court sentencing them to serve a maximum term of imprisonment of more than six (6) years;

(3) Persons who have been convicted by final judgment of the court for violation of banking laws, rules and regulations;

(4) Persons who have been judicially declared insolvent, spendthrift or incapacitated to contract;

(5) Directors/trustees, officers or employees of closed QBs who were found to be culpable for such institution's closure as determined by the Monetary Board;

(6) Directors/trustees and officers of QBs found by the Monetary Board as administratively liable for violation of banking laws, rules and regulations where a penalty of removal from office is imposed, and which finding of the Monetary Board has become final and executory; or

(7) Directors/trustees and officers of QBs or any person found by the Monetary Board to be unfit for the position of directors trustees or officers because they were found administratively liable by another government agency for violation of banking laws, rules and regulations or any offense/violation involving dishonesty or breach of trust, and which finding of said

government agency has become final and executory.

b. *Temporarily disqualified*

Directors/trustees/officers/employees disqualified by the Monetary Board from holding a director/trustee position for a specific/indefinite period of time. Included are:

(1) Persons who refuse to fully disclose the extent of their business interest or any material information to the appropriate department of the SES when required pursuant to a provision of law or of a circular, memorandum, rule or regulation of the BSP. This disqualification shall be in effect as long as the refusal persists;

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(2) Directors/trustees who have been absent or who have not participated for whatever reasons in more than fifty percent (50%) of all meetings, both regular and special, of the board of directors/trustees during their incumbency, and directors/ trustees who failed to physically attend for whatever reasons in at least twenty-five percent (25%) of all board meetings in any year, except that when a notarized certification executed by the corporate secretary has been submitted attesting that said directors/trustees were given the agenda materials prior to the meeting and that their comments/decisions thereon were submitted for deliberation/discussion and were taken up in the actual board meeting, said directors/trustees shall be considered present in the board meeting. This disqualification applies only for purposes of the immediately succeeding election;

(3) Persons who are delinquent in the payment of their obligations as defined hereunder:

(a) *Delinquency in the payment of obligations* means that an obligation of a person with a QB/trust entity where he is a director/trustee or officer, or at least two (2) obligations with other QBs/trust entities/FIs, under different credit lines or loan contracts, are past due pursuant to Secs. X306, 4306Q, 4306S and 4303P;

(b) *Obligations* shall include all borrowings from a QB/trust entity/FI obtained by:

(i) A director/trustees or officer for his own account or as the representative or agent of others or where he acts as a guarantor, indorser or surety for loans from such FIs;

(ii) The spouse or child under parental authority of the director/trustee or officer;

(iii) Any person whose borrowings or loan proceeds were credited to the account of, or used for the benefit of, a director/ trustee or officer;

(iv) A partnership of which a director/ trustee or officer, or his spouse is the managing partner or a general partner owning a controlling interest in the partnership; and

(v) A corporation, association or firm wholly-owned or majority of the capital of which is owned by any or a group of persons mentioned in the foregoing Items *"(i)"*, *"(ii)"* and *"(iv)"*;

This disqualification shall be in effect as long as the delinquency persists.

(4) Persons who have been convicted by a court for offenses involving dishonesty or breach of trust such as, but not limited to, estafa, embezzlement, extortion, forgery, malversation, swindling, theft, robbery, falsification, bribery, violation of B.P. Blg. 22, violation of Anti-Graft and Corrupt Practices Act and prohibited acts and transactions under Section 7 of R.A. No. 6713 (Code of Conduct and Ethical Standards for Public Officials and Employees), violation of banking laws, rules and regulations or those sentenced to serve a maximum term of imprisonment of more than six (6) years but whose conviction has not yet become final and executory;

(5) Directors/trustees and officers of closed QBs/trust entities pending their clearance by the Monetary Board;

(6) Directors/trustees disqualified for failure to observe/discharge their duties and responsibilities prescribed under existing regulations. This disqualification applies until the lapse of the specific period of disqualification or upon approval by the Monetary Board on recommendation by the appropriate department of the SES of such directors'/trustees' election/re-election;

(7) Directors/trustees who failed to attend the special seminar for board of

directors/trustees required under Item *"c"* of Subsec. 4141Q.2. This disqualification applies until the director/trustee concerned had attended such seminar;

(8) Persons dismissed from employment for cause. This disqualification shall be in effect until they have cleared themselves of involvement in the alleged irregularity or upon clearance, on their request, from the Monetary Board after showing good and justifiable reasons, or after the lapse of five (5) years from the time they were officially advised by the appropriate department of the SES of their disqualification;

(9) Those under preventive suspension;

(10) Persons with derogatory records as certified by, or on the official files of, the judiciary, National Bureau of Investigation (NBI), Philippine National Police (PNP), quasi-judicial bodies, other government agencies, international police, monetary authorities and similar agencies or authorities of foreign countries for irregularities or violations of any law, rules and regulations that would adversely affect the integrity of the director/trustee/officer or the ability to effectively discharge his duties. This disqualification applies until they have cleared themselves of the alleged irregularities/violations or after a lapse of five (5) years from the time the complaint, which was the basis of the derogatory record, was initiated;

(11) Directors/trustees and officers of QBs found by the Monetary Board as administratively liable for violation of banking laws, rules and regulations where a penalty of removal from office is imposed, and which finding of the Monetary Board is pending appeal before the appellate court, unless execution or enforcement thereof is restrained by the court;

(12) Directors/trustees and officers of QBs or any person found by the Monetary Board to be unfit for the position of director/trustee or officer because they were found administratively liable by another government agency for violation of banking laws, rules and regulations or any offense/violation involving dishonesty or breach of trust, and which finding of said government agency is pending appeal before the appellate court, unless execution or enforcement thereof is restrained by the court; and

(13) Directors/trustees and officers of QBs found by the Monetary Board as administratively liable for violation of banking laws, rules and regulations where a penalty of suspension from office or fine is imposed, regardless whether the finding of the Monetary Board is final and executory or pending appeal before the appellate court, unless execution or enforcement thereof is restrained by the court. The disqualification shall be in effect during the period of suspension or so long as the fine is not fully paid.

(As amended by Circular Nos. 584 dated 28 September 2007 and 513 dated 10 February 2006)

§ 4143Q.2 *Persons disqualified to become officers*

a. The disqualifications for directors/trustees mentioned in Subsec. 4143Q.1 shall likewise apply to officers, except those stated in Items *"b(2)"* and *"b(7)"*.

b. The spouses or relatives within the second degree of consanguinity or affinity are prohibited from holding officership positions across the following functional categories within a QB:

1. Decision making and senior management function, e.g., chairman, president, chief executive officer (CEO), chief operating officer (COO), general manager, and chief financial officer (CFO) other than the treasurer or controller;

2. Treasury function, e.g., Treasurer and Vice President – Treasury;

3. Recordkeeping and financial reporting functions, e.g., controller and chief accountant;

4. Safekeeping of assets, e.g., chief cashier;

5. Risk management function, e.g., chief risk officer;

6. Compliance function, e.g., compliance officer; and

7. Internal audit function, e.g., internal auditor.

The spouse or a relative within the second degree of consanguinity or affinity of any person holding the position of manager, cashier, or accountant of a branch or extension office of a QB or their respective equivalent positions is disqualified from holding or being appointed to any of said positions in the same branch or extension office.

(As amended by Circular No. 699 dated 17 November 2010)

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§ 4143Q.3 ***Effect of non-possession of qualifications or possession of disqualifications.*** Director/trustee/officer elected or appointed who does not possess all the qualifications mentioned under Subsec. 4141Q.2 and the last paragraph of Sec. 4142Q and/or has any of the disqualifications mentioned under Subsecs. 4143Q.1 and 4143Q.2 shall not be confirmed by the confirming authority under Subsec. 4141Q.4 and shall be removed from office even if he/she assumed the position to which he/she was elected or appointed. Confirmed director/trustee/officer or officer not requiring confirmation possessing any of the disqualifications, as enumerated in the abovementioned subsections shall be subject to the disqualification procedures provided under Subsec. 4143Q.4. Director/trustee/officer, prior to assuming the position to which he/she was elected/appointed, must submit to the appropriate department of the SES a verified statement that he/she has all the aforesaid qualifications and none of the disqualifications. The submission of verified statement will apply to directors/trustees/officers elected/appointed after 14 March 2006.

(As amended by Circular No. 513 dated 10 February 2006)

§ 4143Q.4 ***Disqualification procedures***

a. The board of directors/trustees and management of every institution shall be responsible for determining the existence of the ground for disqualification of the institution's director/trustee/officer or employee and for reporting the same to the BSP. While the concerned institution may conduct its own investigation and impose appropriate sanction/s as are allowable, this shall be without prejudice to the authority of the Monetary Board to disqualify a director/trustee/officer/employee from being elected/appointed as director/trustee/officer in any FI under the supervision of the BSP. Grounds for disqualification made known to the institution, shall be reported to the appropriate department of the SES within seventy-two (72) hours from knowledge thereof.

b. On the basis of knowledge and evidence on the existence of any of the grounds for disqualification mentioned in Subsecs. 4143Q.1 and 4143Q.2, the director/trustee or officer concerned shall be notified in writing either by personal service or through registered mail with registry return receipt card at his/her last known address by the appropriate department of the SES of the existence of the ground for his/her disqualification and shall be allowed to submit within fifteen (15) calendar days from receipt of such notice an explanation on why he/she should not be disqualified and included in the watchlisted file, together with the evidence in support of his/her position. The head of said department may allow an extension on meritorious ground.

c. Upon receipt of the reply/explanation of the director/trustee/officer concerned, the appropriate department of the SES shall proceed to evaluate the case. The director/trustee/officer concerned shall be afforded the opportunity to defend/clear himself/herself.

d. If no reply has been received from the director/trustee/officer concerned upon the expiration of the period prescribed under Item *"b"* above, said failure to reply shall be deemed a waiver and the appropriate department of the SES shall proceed to evaluate the case based on available records/evidence.

e. If the ground for disqualification is delinquency in the payment of obligation, the concerned director/trustee or officer shall be given a period of thirty (30) calendar days within which to settle said obligation or, restore it to its current status or, to explain why he/she should not be

disqualified and included in the watchlisted file, before the evaluation on his disqualification and watchlisting is elevated to the Monetary Board.

f. For directors/trustees/officers of closed banks, the concerned department of the SES shall make appropriate recommendation to the Monetary Board clearing said directors/trustees/officers when there is no pending case/complaint or evidence against them. When there is evidence that a director/trustee/officer has committed irregularity, the appropriate department of the SES shall make recommendation to the Monetary Board that his/her case be referred to the Office of Special Investigation (OSI) for further investigation and that he/she be included in the masterlist of temporarily disqualified persons until the final resolution of his/her case. Directors/trustees/officers with pending cases/complaints shall also be included in said masterlist of temporarily disqualified persons upon approval by the Monetary Board until the final resolution of their cases. If the director/trustee/officer is cleared from involvement in any irregularity, the appropriate department of the SES shall recommend to the Monetary Board his/her delisting. On the other hand, if the director/trustee/officer concerned is found to be responsible for the closure of the institution, the concerned department of the SES shall recommend to the Monetary Board his/her delisting from the masterlist of temporarily disqualified persons and his/her inclusion in the masterlist of permanently disqualified persons.

g. If the disqualification is based on dismissal from employment for cause, the appropriate department of the SES shall, as much as practicable, endeavor to establish the specific acts or omissions constituting the offense or the ultimate facts which resulted in the dismissal to be able to determine if the disqualification of the director/trustee/officer concerned is warranted or not. The evaluation of the case shall be made for the purpose of determining if disqualification would be appropriate and not for the purpose of passing judgment on the findings and decision of the entity concerned. The appropriate department of the SES may decide to recommend to the Monetary Board a penalty lower than disqualification (e.g., reprimand, suspension, etc.) if, in its judgment the act committed or omitted by the director/trustee/officer concerned does not warrant disqualification.

h. All other cases of disqualification, whether permanent or temporary shall be elevated to the Monetary Board for approval and shall be subject to the procedures provided in Items *"a","b","c"* and *"d"* above.

i. Upon approval by the Monetary Board, the concerned director/trustee/officer shall be informed by the appropriate department of the SES in writing either by personal service or through registered mail with registry return receipt card, at his/her last known address of his/her disqualification from being elected/appointed as director/trustee/officer in any FI under the supervision of BSP and/or of his/her inclusion in the masterlist of watchlisted persons so disqualified.

j. The board of directors/trustees of the concerned institution shall be immediately informed of cases of disqualification approved by the Monetary Board and shall be directed to act thereon not later than the following board meeting. Within seventy-two (72) hours thereafter, the corporate secretary shall report to the Governor of the BSP through the appropriate department of the SES the action taken by the board on the director/trustee/officer involved.

k. Persons who are elected or appointed as director/trustee or officer in any of the BSP-supervised institutions for

the first time but are subject to any of the grounds for disqualification provided for under Subsecs. 4143Q.1 and 4143Q.2, shall be afforded the procedural due process prescribed above.

l. Whenever a director/trustee/officer is cleared in the process mentioned under Item *"c"* above or, when the ground for disqualification ceases to exist, he/she would be eligible to become director/trustee or officer of any bank, QB, trust entity or any institution under the supervision of the BSP only upon prior approval by the Monetary Board. It shall be the responsibility of the appropriate department of the SES to elevate to the Monetary Board the lifting of the disqualification of the concerned director/trustee/officer and his/her delisting from the masterlist of watchlisted persons.
(As amended by Circular No. 584 dated 28 September 2007)

§ 4143Q.5 *Watchlisting.* To provide the BSP with a central information file to be used as reference in passing upon and reviewing the qualifications of persons elected or appointed as director/trustee or officer of a bank, QB or trust entity, the SES shall maintain a watchlist of persons disqualified to be a director/trustee or officer of such entities under its supervision under the following procedures:

a. *Watchlist categories*. Watchlisting shall be categorized as follows:

(1) Disqualification File "A" (Permanent)

- Directors/trustees/officers/ employees permanently disqualified by the Monetary Board from holding a director/ trustee/officer position.

(2) Disqualification File "B" (Temporary)

- Directors/trustees/officers/ employees temporarily disqualified by the Monetary Board from holding a director/ trustee/officer position.

b. *Inclusion of directors/trustees/ officers/employees in the watchlist*. Directors/trustees/officers/employees disqualified under Subsec. 4143Q.4 included in the watchlist disqualification files "A" or "B".

c. *Confidentiality*. Watchlist files shall be for internal use only of the BSP and may not be accessed or queried upon by outside parties including banks, QBs and trust entities except with the authority of the person concerned and with the approval of the Deputy Governor, SES or the Governor or the Monetary Board.

BSP will disclose information on its watchlist files only upon submission of a duly accomplished and notarized authorization from the concerned person and approval of such request by the Deputy Governor, SES or the Governor or the Monetary Board. The prescribed authorization form to be submitted to the concerned department of SES is *Appendix Q-45*.

QBs can gain access to information in the said watchlist for the sole purpose of screening their applicants for hiring and/or confirming their elected directors/trustees and appointed officers. QBs must obtain the said authorization on an individual basis.

d. *Delisting*. All delistings shall be approved by the Monetary Board upon recommendation of the operating departments of SES except in cases of persons known to be dead where delisting shall be automatic upon proof of death and need not be elevated to the Monetary Board. Delisting may be approved by the Monetary Board in the following cases:

(1) Watchlist - Disqualification File "B" (Temporary)

(a) After the lapse of the specific period of disqualification;

(b) When the conviction by the court for crimes involving dishonesty, breach of

trust and/or violation of banking law becomes final and executory, in which case the director/trustee/officer/employee is relisted to Watchlist - Disqualification File "A" (Permanent); and

(c) Upon favorable decision or clearance by the appropriate body, i.e., court, NBI, BSP, bank, QB, trust entity or such other agency/body where the concerned individual had derogatory record.

Directors/trustees/officers/employees delisted from the Watchlist

- Disqualification File "B" other than those upgraded to Watchlist
- Disqualification File "A" shall be eligible for re-employment with any bank, QB or trust entity.

(As amended by CL-2007-001 dated 04 January 2007 and CL-2006-046 dated 21 December 2006)

§ 4143Q.6 *Prohibition against foreign officers/employees of financing companies.* Except in the case of technical personnel whose employment may be specifically authorized by the Secretary of Justice, foreigners cannot be officers or employees of financing companies.

Sec. 4144Q *(2008 - 4146Q)* Monetary Board Confirmation of Directors/Trustees and Senior Officers. The election/appointment of directors/trustees and officers with the rank of senior vice-president and up shall require confirmation by the Monetary Board.

The election/appointment of the directors/trustees and such officers shall be deemed to have been confirmed by the Monetary Board if after sixty (60) business days from receipt of the reports required in *Appendix Q-3* by the BSP, no advice against said election/appointment has been received by the QB concerned.

If the Monetary Board finds grounds for disqualification, the director/trustee/officer so elected/appointed may be removed from office even if he/she has assumed the position to which he/she was elected appointed pursuant to Section 9-A of R.A. No. 337, as amended.

Sec. 4145Q *(2008 - 4144Q)* Interlocking Directorships and/or Officerships. In order to safeguard against the excessive concentration of economic power, unfair competitive advantage or conflict of interest situations to the detriment of others through the exercise by the same person or group of persons of undue influence over the policy-making and/or management functions of similar FIs while at the same time allowing banks, QBs and NBFIs without quasi-banking functions to benefit from organizational synergy or economies of scale and effective sharing of managerial and technical expertise, the following regulations shall govern interlocking directorships and/or officerships within the financial system consisting of banks, QBs and NBFIs.

For purposes of this Section, QBs shall refer to IHs, finance companies, trust entities and all other NBFIs with quasi-banking functions while NBFIs shall refer to IHs, finance companies, trust entities, insurance companies, securities dealers/brokers, credit card companies, NSSLAs, holding companies, investment companies, government NBFIs, asset management companies, insurance agencies/brokers, venture capital corporations, FX dealers, money changers (MCs), lending investors, pawnshops, fund managers, mutual building and loan associations, remittance agents and all other NBFIs without quasi-banking functions.

a. *Interlocking directorships* While concurrent directorship may be the least prejudicial of the various relationships cited in this Section to the interests of the FIs involved, certain measures are still necessary to safeguard against the

disadvantages that could result from indiscriminate concurrent directorship.

(1) Except as may be authorized by the Monetary Board or as otherwise provided hereunder, there shall be no concurrent directorships between QBs or between a QB and a bank; and

(2) Without the need for prior approval of the Monetary Board, concurrent directorships between entities not involving an IH shall be allowed in the following cases:

(a) A QB and a bank without quasi-banking functions; and

(b) A bank and one (1) or more of its subsidiary bank/s, QB/s, and NBFI/s; and

(c) A QB and an NBFI.

For purposes of the foregoing, a husband and his wife shall be considered as one (1) person.

b. *Interlocking directorships and officerships*

In order to prevent any conflict of interest resulting from the exercise of directorship coupled with the reinforcing influence of an officer's decision-making and implementing powers, the following rules shall be observed.

(1) Except as may be authorized by the Monetary Board or as otherwise provided hereunder, there shall be no concurrent directorship and officership between QBs, or between a QB and a bank, and between a QB and an NBFI.

(2) Without the need for prior approval of the Monetary Board, concurrent directorship and officership shall be allowed in the following cases:

(a) Between a QB and one (1) or more of its subsidiary QB/s and NBFI/s;

(b) Between a QB, other than an investment house and one (1) or more of its subsidiary banks, QBs and NBFI/s other than investment house/s; and

(c) Between a bank and one (1) or more of its subsidiary bank/s, QB/s, and NBFIs, other than investment house/s.

c. *Interlocking officerships*

A concurrent officership in different FIs may present more serious problems of self-dealing and conflict of interest. Multiple positions may result in poor governance or unfair competitive advantage. Considering the full-time nature of officer positions, the difficulties of serving two (2) offices at the same time, and the need for effective and efficient management, the following rules shall be observed:

As a general rule, there shall be no concurrent officerships, including secondments, between QBs or between a QB and a bank or between a QB and an NBFI. For this purpose, *secondment* shall refer to the transfer/detachment of a person from his regular organization for temporary assignment elsewhere where the seconded employee remains the employee of the home employer although his salaries and other remuneration may be borne by the host organization.

However, subject to prior approval of the Monetary Board, concurrent officerships, including secondments, may be allowed in the following cases:

(1) Between a QB, other than an IH, and not more than two (2) of its subsidiary bank/s, QB/s,and NBFI/s other than IH/s; or

(2) Between two (2) QBs, or between a QB, other than an IH, and a bank, or between a QB and an NBFI: *Provided*, That at least twenty percent (20%) of the equity of each of the banks, QBs or NBFIs is owned by a holding company or a QB/bank and the interlocking arrangement is necessary for the holding company or the QB/bank to provide technical expertise or managerial assistance to its subsidiaries/ affiliates.

(3) Between a QB and not more than two (2) of its subsidiary QB/s, and NBFI/s; or

(4) Between a bank and not more than

two (2) of its subsidiary bank/s, QB/s, and NBFIs, other than IH/s; or

(5) Between a bank and not more than two (2) of its subsidiary QB/s, and NBFI/s.

Aforementioned concurrent officerships may be allowed, subject to the following conditions:

(a) that the positions do not involve any functional conflict of interests;

(b) that any officer holding the positions of president, CEO, chief operating officer or chief financial officer may not be concurrently appointed to any of said positions or their equivalent;

(c) that the officer involved, or his spouse or any of his relatives within the first degree of consanguinity or affinity or by legal adoption, or a corporation, association or firm wholly-or majority owned or controlled by such officer or his relatives enumerated above, does not own in his/its own capacity more than twenty percent (20%) of the subscribed capital stock of the entities in which the QB has equity investments; and

(d) that where any of the positions involved is held on full-time basis, adequate justification shall be submitted to the Monetary Board.

(6) Concurrent officership position in the same capacity which do not involve management functions, i.e., internal auditors, corporate secretary, assistant corporate secretary and security officer, between a QB and one or more of its subsidiary QB/s and NBFI/s, or between a bank and one or more of its subsidiary QBs and NBFIs, or between bank/s, QB/s and NBFI/s, other than IH/s: *Provided*, That at least twenty percent (20%) of the equity of each of the banks, QBs and NBFIs is owned by a holding company or by any of the banks/QBs within the group.

For purposes of this Section, members of a group or committee, including sub-groups or sub-committees, whose duties include functions of management such as those ordinarily performed by regular officers, shall likewise be considered as officers.

It shall be the responsibility of the Corporate Governance Committee to conduct an annual performance evaluation of the board of directors/trustees and senior management. When a director/trustee or officer has multiple positions, the Committee should determine whether or not said director/trustee or officer is able to and has been adequately carrying out his/her duties and, if necessary, recommend changes to the board based upon said performance/review.

(As amended by Circular Nos. 646 dated 23 February 2009 and 592 dated 28 December 2007)

§ 4145Q.1 ***(2008 - 4144Q.1) Representatives of government.*** The provisions of this Subsection shall apply to persons appointed to such positions as representatives of the government or government-owned or controlled entities unless otherwise provided under existing laws.

(As amended by Circular No. 592 dated 28 December 2007)

Sec. 4146Q ***(2008 - 4145Q)*** **Profit Sharing of Directors/Trustees/Officers and Employees.** Profit sharing programs adopted in favor of directors/trustees/officers and employees shall be reflected in the by-laws of QBs, subject to the following guidelines:

a. The base in any profit sharing program shall be the net income for the year of the QB, as shown in its Consolidated Statement of Income and Expenses (CSIE) for the year, net of the following:

(1) All cumulative dividends accruing to preferred stock to the extent not covered by earned surplus;

(2) Accrued interest receivable credited to income but not yet collected, net of reserves already set up for uncollected interest on loans;

schedule approved by the Monetary Board, as well as all amortizations due on deferred charges;

(4) Provisions for the current year's taxes;

(5) Income tax deferred for the year: *Provided, however,* That in case of reversal of deferred income taxes excluded from net income in previous years' profit sharings, the deferred income tax reversed to expense shall be added back to net income to arrive at the basis for profit sharing for the year during which the reversal is made;

(6) Accumulated profits not yet received but already recorded by a QB representing its share in profits of its subsidiaries under the equity method of accounting; and

b. The QB may provide in its by-laws for other priorities in the computation of net profits for purposes of profit sharing: *Provided,* That in no case shall profit sharing take precedence over any of the items in the preceding paragraph.

Sec. 4147Q Compensation and Other Benefits of Directors/Trustees and Officers. To protect the funds of creditors, the Monetary Board may regulate/restrict the payment by the QB/trust entity of compensation, allowances, fees, bonuses, stock options, profit sharing and fringe benefits to its directors/trustees and officers in exceptional cases and when the circumstances warrant, such as, but not limited to, the following:

a. When the QB/trust entity is under controllership, conservatorship or when it has outstanding emergency loans and advances and such other forms of credit accommodation from the BSP which are intended to provide it with liquidity in times of need;

b. When the institution is found by the Monetary Board to be conducting business in an unsafe or unsound manner; and

c. When it is found by the Monetary Board to be in an unsatisfactory financial condition such as, but not limited to, the following cases:

(1) Its capital is impaired;

(2) It has suffered continuous losses from operations for the past three (3) years;

(3) Its composite CAMELS rating in the latest examination is below "3"; and

(4) It is under rehabilitation by the BSP/PDIC which rehabilitation may include debt-to-equity conversion, etc.

In the presence of any one (1) or more of the circumstances mentioned above, the Monetary Board may impose the following restrictions in the compensation and other benefits of directors and officers:

a. In the case of profit sharing, the provision of Sec. 4146Q shall be observed except that for purposes of this Section, the total amount of unbooked valuation reserves and deferred charges shall be deducted from the net income.

b. Except for the financial assistance to meet expenses for the medical, maternity, education and other emergency needs of the directors/trustees or officers or their immediate family, the other forms of financial assistance may be suspended.

c. When the total compensation package including salaries, allowances, fees and bonuses of directors/trustees and officers are significantly excessive as compared with peer group averages, the Monetary Board may order their reduction to reasonable levels: *Provided*, That even if a QB/trust entity is in financial trouble, it may nevertheless be allowed to grant relatively higher salary packages in order to attract competent officers and quality staff as part of its rehabilitation program.

The foregoing provisions founded on Section 18 of R.A. No. 8791 shall be deemed part of the benefits and compensation programs of QBs/trust entities.

Sec. 4148Q (Reserved)

Sec. 4149Q Conducting Business in an Unsafe/Unsound Manner. Whether a particular activity may be considered as conducting business in an unsafe or unsound manner, all relevant facts must be considered. An analysis of the impact thereof on the QB's/trust entity's operations and financial conditions must be undertaken, including evaluation of capital position, asset condition, management, earnings posture and liquidity position.

In determining whether a particular act or omission, which is not otherwise prohibited by any law, rule or regulation affecting QBs/trust entities, may be deemed as conducting business in an unsafe or unsound manner, the Monetary Board, upon report of the head of the supervising or examining department based on findings in an examination or a complaint, shall consider any of the following circumstances:

a. The act or omission has resulted or may result in material loss or damage, or abnormal risk or danger to the safety, stability, liquidity or solvency of the institution;

b. The act or omission has resulted or may result in material loss or damage or abnormal risk to the institutions, creditors, investors, stockholders, or to the BSP, or to the public in general;

c. The act or omission has caused any undue injury, or has given unwarranted benefits, advantage or preference to the QB/trust entity or any party in the discharge by the director or officer of his duties and responsibilities through manifest partiality, evident bad faith or gross inexcusable negligence; or

d. The act or omission involves entering into any contract or transaction manifestly and grossly disadvantageous to the QB/trust entity, whether or not the director or officer profited or will profit thereby.

The list of activities which may be considered unsafe and unsound is shown in *Appendix Q-24*.

(As amended by Circular No. 640 dated 16 January 2009)

§§ 4149Q.1 - 4149Q.8 *(Reserved)*

§ 4149Q.9 *Sanctions.* The Monetary Board may, at its discretion and based on the seriousness and materiality of the acts or omissions, impose any or all of the following sanctions provided under Section 37 of R.A. No. 7653 and Section 56 of R.A. No. 8791, whenever a QB/trust entity conducts business in an unsafe and unsound manner:

a. Issue an order requiring the QB/trust entity to cease and desist from conducting business in an unsafe and unsound manner and may further order that immediate action be taken to correct the conditions resulting from such unsafe or unsound practice;

b. Fines in amounts as may be determined by the Monetary Board to be appropriate, but in no case to exceed P30,000 a day on a per transaction basis taking into consideration the attendant circumstances, such as the gravity of the act or omission and the size of the QB/trust entity, to be imposed on the QB/trust entity, their directors and/or responsible officers;

c. Suspension of lending or FX operations or authority to accept new deposit substitutes and/or new trust accounts or to make new investments;

d. Suspension of responsible directors and/or officers;

e. Revocation of quasi-banking license and/or trust authority; and/or

f. Receivership and liquidation under Section 30 of R.A. No. 7653.

All other provisions of Sections 30 and 37 of R.A. No. 7653, whenever appropriate, shall also be applicable on the conduct of business in an unsafe or unsound manner.

The imposition of the above sanctions is without prejudice to the filing of appropriate criminal charges against culpable persons as provided in Sections 34, 35 and 36 of R.A. No. 7653.

Sec. 4150Q Rules of Procedure on Administrative Cases Involving Directors and Officers of Quasi-Banks. The rules of procedure on administrative cases involving directors and officers of QBs are shown in *Appendix Q-35*.

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I. BRANCHES AND OTHER OFFICES

Sec. 4151Q Establishment. Prior BSP authority shall be obtained before operating a branch, extension office or agency, including any arrangement whereby another person or entity is authorized to act as an agent for solicitation, issuance or servicing of deposit substitutes for the QB.

Agency arrangements shall refer to all or any type of services to be performed by another party as an agent other than collection agency for loans payable in installments/amortization, and paying agency under a definite and specific period for purposes of redeeming long-term notes and/or bonds.

§ 4151Q.1 ***Evaluation guideposts***. The rate at which branches, agencies, extension offices, etc. are to be established shall depend upon the ability of the company to conduct operations from the head office, as well as correspondent/banking arrangements.

§ 4151Q.2 ***Additional capital, if required.*** An applicant QB may be required to put up additional capital in an amount to be determined by the appropriate department of the SES, based on criteria which consider expected growth of risk assets and capital accounts and for this purpose, the methods of computing such additional capital, as shown in *Appendix Q-2,* shall be used.

§ 4151Q.3 ***Other requirements/factors to be considered.*** Other requirements/ factors to be considered are the applicant QB's general compliance with laws, rules, and regulations, and policies of the BSP, such as:

a. Capital adequacy and solvency;

b. Profitability and capacity to absorb losses; and

c. Reserve and liquidity position.

§ 4151Q.4 ***Conditions precluding processing of applications.*** The existence of any of the following conditions shall preclude/suspend the processing of the application:

a. The applicant has not complied with the ceilings on credit accommodations to DOSRI during the last sixty (60) days immediately preceding the date of application;

b. The net worth of the applicant is found to be deficient during the last sixty (60) days immediately preceding the date of application; and

c. The applicant has incurred net deficiencies in reserves against deposit substitute liabilities during the last eight (8) weeks immediately preceding the date of application.

§ 4151Q.5 ***Documentary requirements*** All applications shall be supported by the following documents:

a. Ability to conduct operations from the head office as not to be a cause for delayed submission of reports to the BSP and/or recording of transactions in the head office;

b. Correspondent banking and audit arrangements between the branch and the head office to ensure effective and efficient cash/money transactions;

c. Certified true copy of the board resolution authorizing the establishment of a branch;

d. Services to be offered, as well as any extension offices, etc. to be opened;

e. Days and hours to be observed;

f. Areas to be served;

g. Bio-data of the proposed branch manager and organizational chart;

h. Business and/or economic justifications (including data) for the establishment of the branch; and

i. Number of FIs in the area (banks, IHs, finance companies and pawnshops).

§ 4151Q.6 ***Filing of applications*** Applications for a certificate of authority to operate a branch, an extension office or an agency shall be filed with the SEC, which office shall refer the same to the appropriate department of the SES for comments and recommendations. A copy of the application filed with the SEC, with the pertinent documents, shall simultaneously be furnished the appropriate department of the SES for advance verification of the QB's compliance with the requirements under the provisions of Sec. 4151Q.

§ 4151Q.7 ***Period within which to submit complete requirements.*** The applicant QB shall have one (1) month from notice of the receipt of the SEC referral by the appropriate department of the SES within which to submit/complete the requirements under this Section, after which the non-submission of complete documents shall cause the return of the application for the QB's lack of interest to pursue the same.

§ 4151Q.8 ***Prohibition against operating without Securities and Exchange Commission license.*** No branch, extension office or agency shall start operations unless the appropriate SEC license, which likewise serves as authorization for the branch/ extension office/agency to perform quasi-banking functions, has been issued.

Secs. 4152Q - 4155Q (Reserved)

J. (RESERVED)

Secs. 4156Q - 4159Q (Reserved)

K. BANKING PREMISES

Sec. 4160Q ***(2008 - 4651Q)*** **Quasi-Bank Premises and Other Fixed Assets.** The following rules shall govern the premises and other fixed assets of QBs.

§ 4160Q.1 ***(2008 - 4651Q.1) Appreciation or increase in book value.*** QB premises, furniture, fixtures and equipment shall be accounted for using the cost model under Philippine Accounting Standards (PAS) 16 "Property, Plant and Equipment." Outstanding appraisal increment as of 13 October 2005 arising from mergers and consolidation and other cases approved by the Monetary Board, shall be deemed part of the cost of the assets. However, appraisal increment previously allowed to be booked shall be reversed.

Accordingly, the booking of appreciation or increase in the book value of QB premises and other fixed assets in cases where the market value of the property has greatly increased since the original purchase is no longer allowed.

(As amended by Circular No. 520 dated 20 March 2006)

§ 4160Q.2 ***(Reserved)***

§ 4160Q.3 ***(2008 - 4651Q.3) Reclassification of real and other properties acquired to QB premises, furniture, fixture and equipment; Sanctions.*** QBs may reclassify ROPA to QB premises, furniture, fixture and equipment, subject to the following conditions:

(a) Prior written approval of the majority of the members of the board of directors has been obtained for such reclassification. The approval shall be manifested in a resolution passed by the board of directors during a meeting and shall contain the following information:

(1) Date ROPA was acquired;

(2) Description of ROPA property;

(3) Outstanding balance of ROPA at the time of reclassification;

(4) Specific purpose for reclassifying said property to QB premises, furniture, fixture and equipment; and

(5) Justification and plan for expansion, in the case of real and other property earmarked for future use.

Said resolution shall also be made available for inspection by BSP examiners, together with the supporting records and documents involving the ROPA account; and

(b) Only such acquired asset, or a portion thereof, that will be (i) immediately used, or (ii) ready and available for use within a two (2)-year period from date of reclassification (in case of ROPA earmarked for future use) may be reclassified to QB premises, furniture, fixture and equipment;

(c) ROPA reclassified to QB Premises, Furniture, Fixture and Equipment shall be recorded at its net carrying amount where the amounts booked as cost, accumulated depreciation and allowances for losses for QB Premises, Furniture, Fixture and Equipment shall correspond to the balance of these accounts under ROPA at the time of reclassification. As such, the reclassification shall not give rise to any gains/(losses) being recognized in the QB books; and

(d) Said reclassification shall not cause the QB to exceed the prescribed ceiling on investment in real estate and improvements thereon, including QB equipment, provided under Subsec. X160.2.

Within five (5) business days from date of reclassification, the QB shall submit the Certification on Compliance with Regulations on the Reclassification of ROPA to QB Premises, Furniture, Fixture and Equipment (*Appendix Q-54*) signed by the president of the QB or officer of equivalent rank, to the appropriate department of the SES. Said certification shall be accompanied by the certified true copy of the resolution of the QB's board of directors authorizing the reclassification.

Sanctions. The following sanctions shall be imposed for violations noted:

1. On the QB

a. Monetary fines

A QB which fails to comply with the provisions of this Subsec. shall be subject to monetary penalties under *Appendix Q-39*.

1) For non-submission of the required certification

A QB which fails to submit the required Certification on Compliance with Regulations on the ROPA to QB Premises, Furniture, Fixture and Equipment or the certified true copy of the resolution of the board of directors authorizing said reclassification within the prescribed deadline shall be subject to monetary penalties applicable to minor offenses under *Appendix Q-39* which shall be reckoned on a daily basis from the day following the due date of submission until the required certification on compliance or the certified true copy of the resolution of the board of directors is filed with the BSP.

2) For false/misleading statements

A QB which has been found to have willfully made a false or misleading statement in the required Certification on Compliance with Rules and Regulations on the ROPA to QB Premises, Furniture, Fixture and Equipment or in the certified true copy of the resolution of the QB board of directors shall be subject to the monetary penalties applicable to minor offenses under *Appendix Q-39* for the willful making of a false or misleading statement which shall be reckoned on a daily basis from the day following the due date of the said certification until such time that an amended

or corrected certification on compliance or certified true copy of the resolution of the board of directors has been submitted to the BSP.

2. On the concerned directors/officers of the bank

a. For willful non-compliance

Directors/officers of the QB who willfully fail/refuse to comply with the provisions of this Subsection shall be subject to the monetary penalties applicable to minor offenses under *Appendix Q-39*.

b. For false/misleading statements

Directors/officers of the QB which have been found to have willfully falsely certified or willfully submitted misleading statements in the required Certification on Compliance with the Regulation on the Reclassification of ROPA to QB Premises, Furniture, Fixture and Equipment or in the certified true copy of the resolution of the QB's board of directors shall be subject to the monetary penalties applicable to minor offenses under *Appendix Q-39*, which shall be reckoned on a daily basis from the day following the due date of the said certification until such time that an amended or corrected certification on compliance or certified true copy of the resolution of the board of directors has been submitted to the BSP.

The imposition of the above sanctions is without prejudice to the filing of appropriate criminal charges against culpable persons as provided under Section 35 of R.A. No. 7653 for the willful making of a false/misleading statement.

(As amended by Circular no. 701 dated 13 December 2010)

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§§ 4160Q.4 - 4160Q.9 *(Reserved)*

§ 4160Q.10 *(2008 - 4651Q.9) Batas Pambansa Blg. 344 – An Act to Enhance the Mobility of Disabled Persons by Requiring Certain Buildings, Institutions, Establishments and Public Utilities to Install Facilities and Other Devices.* In order to promote the realization of the rights of disabled persons to participate fully in the social life and the development of the societies in which they live and the enjoyment of the opportunities available to other citizens, no license or permit for the construction, repair or renovation of public and private buildings for public use, educational institutions, airports, sports and recreation centers and complexes, shopping centers or establishments, public parking places, workplaces, public utilities, shall be granted or issued unless the owner or operator thereof shall install and incorporate in such building, establishment or public utility, such architectural facilities or structural features as shall reasonably enhance the mobility of disabled persons such as sidewalks, ramps, railings and the like. If feasible, all such existing buildings, institutions, establishments, or public utilities may be renovated or altered to enable the disabled persons to have access to them.

L. MANAGEMENT CONTRACTS AND OUTSOURCING OF BANKING FUNCTIONS

Sec. 4161Q *(2008 - 4182Q)* Management Contracts. Subject to existing laws, all agreements whereby the affairs or operations of a QB will be carried out by another corporation, person or group of persons, shall be subject to prior approval by the BSP.

The agreements referred to in the preceding paragraph shall not be entered into for a period longer than five (5) years. Existing agreements shall be allowed up to the termination date thereof: *Provided, however,* That any renewal or extension upon termination date shall be subject to approval by the BSP.

Sec. 4162Q *(2008 - 4190Q)* Duties and Responsibilities of Quasi-Banks and their Directors/Officers in All Cases of Outsourcing of Quasi-Banking Functions The rules on outsourcing of banking functions as shown in *Appendix Q-37* shall be adopted in so far as they are applicable to QBs.

(As amended by Circular Nos. 642 dated 30 January 2009, 610 dated 26 May 2008, 596 dated 11 January 2008, 548 dated 25 September 2006 and 543 dated 08 September 2006)

Sec. 4163Q - 4167Q (Reserved)

M. (RESERVED)

Sec. 4168Q - 4172Q (Reserved)

N. RISK MANAGEMENT

Sec. 4173Q *(2008 - 4193Q)* Supervision by Risks. The guidelines on supervision by risk to provide guidance on how QBs should identify, measure, monitor and control risks are shown in *Appendix Q-42*.

The guidelines set forth the expectations of the BSP with respect to the management of risks and are intended to provide more consistency in how the risk-focused supervision function is applied to these risks. The BSP will review the risks to ensure that a QB's internal risk management processes are integrated and comprehensive. All QBs should follow the guidance in their risk management efforts.

(Circular No. 510 dated 19 January 2006)

Sec. 4174Q *(2008 - 4194Q)* Market Risk Management. The guidelines on market risk management in *Appendix Q-43* set forth the expectations of the BSP with respect to the management of market risk and are intended

to provide more consistency in how the risk-focused supervision function is applied to this risk. QBs are expected to have an integrated approach to risk management to identify, measure, monitor and control risks. Market risk should be reviewed together with other risks to determine overall risk profile.

The BSP is aware of the increasing diversity of financial products and that industry techniques for measuring and managing market risk are continuously evolving. As such, the guidelines are intended for general application; specific application will depend to some extent on the size, complexity and range of activities undertaken by individual QBs.

The guidelines on market risk management are shown in *Appendix Q - 15*.
(Circular No. 544 dated 15 September 2006)

Sec. 4175Q *(2008 - 4195Q)* Liquidity Risk Management. The guidelines on liquidity risk management in *Appendix Q-44* set forth the expectations of the BSP with respect to the management of liquidity risk and are intended to provide more consistency in how the risk-focused supervision function is applied to this risk. QBs are expected to have an integrated approach to risk management to identify, measure, monitor and control risks. Liquidity risk should be reviewed together with other risks to determine overall risk profile.

The guidelines are intended for general application; specific application will depend on the size and sophistication of a particular QB and the nature and complexity of its activities.

The guidelines on liquidity market risk management are shown in *Appendix Q - 15*.
(Circular No. 545 dated 15 September 2006)

Secs. 4176Q - 4179Q (Reserved)

Sec. 4180Q *(2008 - 4191Q)* Compliance System; Compliance Officer. QBs shall develop and implement a compliance system and appoint/designate a compliance officer to oversee its implementation.

§ 4180Q.1 *(2008 - 4191Q.1) Compliance system.* The compliance system shall have the following basic elements.

a. A written compliance program approved by the board of directors:

(1) The compliance program shall enable the QB to identify the relevant Philippine laws and regulations, analyze the corresponding risks of non-compliance, and prioritize the compliance risks (e.g., low, medium, high).

(2) The program shall provide for periodic compliance testing with applicable legal and regulatory requirements. Testing frequency shall be commensurate with identified risk levels (e.g., annual testing for low-risk, quarterly testing for medium-risk, monthly testing for high-risk). It shall also provide for the reporting of compliance findings noted to appropriate levels of management.

(3) The program shall establish the responsibilities and duties of the compliance officer and other personnel (if any) involved in the compliance function.

(4) A copy of the compliance program and the written approval of the board of directors shall be submitted to the appropriate department of the SES within twenty (20) business days from date of approval.

(5) The program shall be updated at least annually to incorporate changes in laws and regulations. Any changes in the program shall likewise be approved by the QB's board of directors and submitted to BSP within twenty (20) business days from the date of approval.

b. A constructive working relationship with regulatory agencies.

The QB, through its compliance officer, may consult the regulatory agencies for additional clarification on specific provisions of laws and regulations and/or discuss compliance findings with the regulatory authorities. A dialogue may also be initiated with respect to borderline issues.

c. A clear and open communication process within the QB to educate and address compliance matters.

Officers and staff shall be trained on the regulatory requirements through regular meetings, distribution of manuals and dissemination of regulatory issuance.

d. Continuous monitoring and assessment of the compliance program.

The program shall provide for the periodic review of the compliance function to measure its effectiveness. The review may be carried out by the internal audit department of the QB.

The compliance program may operate parallel to or as part of a QB's internal control and auditing program.

§ 4180Q.2 ***(2008 - 4191Q.2) Compliance officer***

a. The principal function of the compliance officer is to oversee and coordinate the implementation of the compliance system. His responsibility shall include the identification, monitoring and controlling of compliance risk.

b. The appointment/designation of a compliance officer shall require prior approval of the Monetary Board. The bio-data of the proposed compliance officer shall be submitted to the appropriate department of the SES.

c. The compliance officer shall have the skills and expertise to provide appropriate guidance and direction to the bank on the development, implementation and maintenance of the compliance program.

d. QBs with total resources of P500 million and above shall appoint an independent full-time compliance officer, who shall have a rank of at least a vice president or its equivalent.

e. For QBs with total resources of below P500 million, an incumbent senior officer may be designated concurrently as the QB's compliance officer: *Provided,* That such designation will not give rise to any conflict of interest situation and that the main function of the senior officer shall be that of a compliance officer.

The internal auditor of a QB may also be designated as its compliance officer subject to the condition that his main function shall be that of a compliance officer.

Transitory provision. Compliance officers concurrently holding the position of Head of Internal Audit or Internal Auditor shall be given one (1) year from 02 February 2008 within which to comply with this Subsection.

(As amended by Circular No. 598 dated 11 January 2008)

§ 4180Q.3 ***(2008 - 4191Q.3) Compliance risk.*** *Compliance risk* is the risk of legal or regulatory sanctions, financial loss, or loss to reputation a QB may suffer as a result of its failure to comply with all applicable laws, regulations, codes of conduct and standards of good practice.

§ 4180Q.4 ***(2008 - 4191Q.4) Responsibilities of the board of directors and senior management on compliance*** Aside from the duties and responsibilities of the board of directors mentioned under Subsec. 4141Q.3, the board should oversee the implementation of the compliance policy and ensure that compliance issues are resolved expeditiously. Senior management should be responsible for establishing a compliance policy, ensuring that it is observed, reporting to the board of

directors on its ongoing implementation and assessing its effectiveness and appropriateness. Senior management should, at least once a year, report to the board of directors or a committee of the board on matters relevant to the compliance policy and its implementation, recommending any required changes to the policy. The report should assist the board members in making an informed assessment as to whether the institution is managing its compliance risk effectively. However, any material breaches of laws, rules and standards shall be reported promptly.

§ 4180Q.5 ***(2008 - 4191Q.5) Status of compliance function.*** The compliance function should have a formal status within the organization established by a charter or other formal document approved by the board of directors that defines the compliance function's standing, authority and independence, and addresses the following issues:

(1) measures to ensure the independence of the compliance function from the business activities of the QB;

(2) its role and responsibilities;

(3) its relationship with other functions or units within the organization;

(4) its right to obtain access to information necessary to carry out its responsibilities;

(5) its right to conduct investigations of possible breaches of the compliance policy;

(6) its formal reporting relationships to senior management and the board of directors; and

(7) its right of direct access to the board of directors or an appropriate committee of the board.

The compliance charter or other formal document defining the status of the compliance function shall be communicated throughout the organization.

§ 4180Q.6 ***(2008 - 4191Q.6) Independence of compliance function*** The compliance function should be independent from the business activities of the institution. It should be able to carry out its responsibilities on its own initiative in all units or departments where compliance risk exists and must be provided with sufficient resources to carry out its responsibilities effectively. It must be free to report to senior management and the board or a committee of the board on any irregularities or breaches of laws, rules and standards discovered, without fear of retaliation or disfavor from management or other affected parties. The compliance function should have access to all operational areas as well as any records or files necessary to enable it to carry out its duties and responsibilities.

§ 4180Q.7 ***(2008 - 4191Q.7) Role and responsibilities of the compliance function*** The role and responsibilities of the compliance function should be clearly defined. If there is a division of duties and responsibilities between different functions such as legal, compliance, internal audit or risk management, the allocation of duties and responsibilities to each function should be properly delineated. There should likewise be formal arrangements for cooperation between each function and for the exchange of relevant information.

§ 4180Q.8 ***(2008 - 4191Q.8) Cross-border issues.*** The compliance function for institutions that conduct business in other jurisdictions should be structured to ensure that local compliance concerns are satisfactorily addressed within the framework of the compliance policy for the organization as a whole. As there are significant differences in legislative and regulatory frameworks across countries or from jurisdiction to jurisdiction, compliance issues specific to each

jurisdiction should be coordinated within the structure of the institution's group-wide compliance policy. The organization and structure of the compliance function and its responsibilities should be in accordance with local legal and regulatory requirements.

§ 4180Q.9 *(2008 - 4191Q.9)*

Outsourcing of compliance function. QBs should establish policies for managing the risks associated with outsourcing activities.

Outsourcing of services/activities can reduce the institution's risk profile by transferring activities to others with the necessary expertise to manage the risks associated with specialized business activities. However, the use of third parties does not diminish the responsibility of the board of directors and senior management to ensure that the outsourced activity is conducted in a safe and sound manner and in compliance with applicable laws and regulations.

Compliance risk assessment and testing may be outsourced, subject to appropriate oversight by the compliance officer: *Provided,* That a copy of the outsourcing agreement stating the duties and responsibilities as well as rights and obligations of the contracting parties, which agreement shall be approved by the board of directors of the institution concerned, must be submitted to the appropriate department of the SES at least thirty (30) days prior to its execution to enable review of its compliance with existing regulations on outsourcing of quasi-banking functions.

The service level agreement shall ensure a clear allocation of responsibilities between the external service providers and the QB. *Furthermore*, the outsourcing QB should manage residual risks associated with outsourcing arrangements, including default, operational failures, and possible disruption of services.

Secs. 4181Q - 4184Q (Reserved)

Sec. 4185Q *(2008 - 4171Q)* Internal Control Systems. The minimum internal control standards established in *Appendix Q-5* shall guide all QBs. The following records/data shall be compiled and made available for the inspection of BSP examiners.

a. Records showing compliance with independent balancing procedures. These records should indicate the accounts and the periodic balancing procedures performed.

b. Statements of actual duties of persons assigned to handle cash and securities.

c. All internal control audit reports or their equivalent.

d. Information/data on the direct and/or indirect equity holdings and/or connection with any firm, partnership or corporation organized for profit, of all the institution's directors, officers, and major stockholders, as defined under Secs. 4141Q and 4142Q.

e. Information/data pertaining to electronic data processing (EDP) department or service bureau of the QB particularly on organization, input control, processing control, output control, software, program and documentation standards, logs on the operations of mainframes and peripherals, hardware control and such other EDP control standards prescribed by the BSP in separate rules and regulations.

§ 4185Q.1 - 4185Q.8 *(Reserved)*

§ 4185Q.9 *(2008 - 4164Q.1)*

Independence of Internal Audit Function The internal audit function must be independent of the activities audited and from day-to-day internal control process. It must be free to report audit results, findings, opinions, appraisals and other information to the appropriate level of management. It shall have authority to

directly access and communicate with any officer or employee, to examine any activity or entity of the institution, as well as to access any records, files or data whenever relevant to the exercise of its assignment. The Audit Committee or senior management should take all necessary measures to provide the appropriate resources and staffing that would enable internal audit to achieve its objectives.

Sec. 4186Q *(2008 - 4164Q)* Internal Audit Function. Internal audit is an independent, objective assurance and consulting function established to examine, evaluate and improve the effectiveness of risk management, internal control, and governance processes of an organization.

§ 4186Q.1 *(Reserved)*

§ 4186Q.2 *(2008 - 4164Q.2) Scope* The scope of internal audit shall include:

a. Examination and evaluation of the adequacy and effectiveness of the internal control systems;

b. Review of the application and effectiveness of risk management procedures and risk assessment methodologies;

c. Review of the management and financial information systems, including the electronic information system and electronic banking services;

d. Assessment of the accuracy and reliability of the accounting system and of the resulting financial reports;

e. Review of the systems and procedures of safeguarding assets;

f. Review of the system of assessing capital in relation to the estimate of organizational risk;

g. Transaction testing and assessment of specific internal control procedures; and

h. Review of the compliance system and the implementation of established policies and procedures.

§ 4186Q.3 *(2008 - 4164Q.3) Qualification standards of the internal auditor.* The internal auditor of a UB or a KB must be a Certified Public Accountant (CPA) and must have at least five (5) years experience in the regular audit (internal or external) of a UB or KB as auditor-in-charge, senior auditor or audit manager. He must possess the knowledge, skills, and other competencies to examine all areas in which the institution operates. Professional competence as well as continuing training and education shall be required to face up to the increasing complexity and diversity of the institution's operations.

The internal auditor of a Thrift Bank (TB), QB, trust entity or national Cooperative Bank (Coop Bank) must be a CPA with at least five (5) years experience in the regular audit (internal or external) of a TB, QB, trust entity or national Coop Bank as auditor-in-charge, senior auditor or audit manager or, in lieu thereof, at least three (3) years experience in the regular audit (internal or external) of a QB as auditor-in-charge, senior auditor or audit manager.

The internal auditor of an RB, NSSLA or local Coop Bank must be at least an accounting graduate with two (2) years experience in external audit or in the regular audit of an Rural Bank (RB), NSSLA or local Coop Bank or, in lieu thereof, at least one (1) year experience in the regular audit (internal or external) of a UB, KB, TB, QB, trust entity or national Coop Bank as auditor-in-charge, senior auditor or audit manager.

A qualified internal auditor of a UB or a KB shall be qualified to audit TBs, QBs, trust entities, national Coop Banks, RBs, NSSLAs, local Coop Banks, subsidiaries and affiliates engaged in allied activities, and other FIs under BSP supervision.

A qualified internal auditor of a TB or national Coop Bank shall likewise be qualified to audit QBs, trust entities, RBs,

NSSLAs, local Coop Banks, subsidiaries and affiliates engaged in allied activities, and other FIs under BSP supervision.

§ 4186Q.4 ***(2008 - 4164Q.4) Code of ethics and internal auditing standards.*** The internal auditor should conform with the Code of Professional Ethics for CPAs and ensure compliance with sound internal auditing standards, such as the Institute of Internal Auditors' *International Standards for the Professional Practice of Internal Auditing* (e-mail: standards@theiia.org; Web: http://www.theiia.org.) and other supplemental standards issued by regulatory authorities/government agencies. The standards address independence and objectivity, professional proficiency, scope of work, performance of audit work, management of internal audit, quality assurance reviews, communication and monitoring of results.

Secs. 4187Q - 4188Q (Reserved)

Sec. 4189Q ***(2008 - 4180Q)*** **Selection, Appointment, Reporting Requirements and Delisting of External Auditors and/or Auditing Firm; Sanction.** Pursuant to Section 58, R.A. No. 8791, and the existing provisions of the executed Memorandum of Agreement (MOA) dated 12 August 2009, binding the BSP, SEC, Professional Regulation Commission (PRC) – Board of Accountancy (BoA) and the Insurance Commission (IC) for a simplified and synchronized accreditation requirements for external auditor and/or auditing firm, following are the revised rules and regulations that shall govern the selection and delisting by the BSP of covered institutions which under special laws are subject to BSP supervision.

Statement of policy. It is the policy of the BSP to ensure effective audit and supervision of banks, QBs, trust entities and/or NSSLAs including their subsidiaries and affiliates engaged in allied activities and other FIs which under special laws are subject to BSP supervision, and to ensure reliance by BSP and the public on the opinion of external auditors and auditing firms by prescribing the rules and regulations that shall govern the selection, appointment, reporting requirements and delisting for external auditors and auditing firms of said institutions, subject to the binding provisions of and implementing regulations pursuant to the aforesaid MOA.

a. *Rules and regulations*. The revised rules and regulations that shall to govern the selection and delisting by the BSP of covered institutions which under special laws are subject to BSP supervision are shown in *Appendix Q-30*.

b. *Sanctions*. The applicable sanctions/penalties prescribed under Sections 36 and 37 of R. A. No. 7653 to the extent applicable shall be imposed on the covered institution, its audit committee and the directors approving the hiring of external auditors/auditing firm who/which are not in the BSP list of selected auditors for covered institution or for hiring, and/or retaining the services of the external auditor/auditing firm in violation of any of the provisions of this Section and for non-compliance with the Monetary Board directive under Item "*K*" in *Appendix Q-30*. Erring external auditors/auditing firm may also be reported by the BSP to the PRC for appropriate disciplinary action.

(As amended by Circular Nos. 660 dated 25 August 2009 and 529 dated 11 May 2006)

Sec. 4190Q ***(2008 - 4172Q)*** **Audited Financial Statements of Quasi-Banks; Financial Audit.** The following rules shall govern the utilization and submission of audited financial statements (AFS) of QBs.

For purposes of this Section, AFS shall include the balance sheets, income statements (IS), statements of changes in equity, statements of cash flows and notes to financial statements which shall include among other information, disclosure of the

volume of past due loans as well as loan-loss provisions. On the other hand, financial audit report (FAR) shall refer to the AFS and the opinion of the auditor. The AFS of QBs with subsidiaries shall be presented side by side on a solo basis (parent) and on a consolidated basis (parent and subsidiaries).

QBs shall cause an annual financial audit by an external auditor acceptable to the BSP not later than thirty (30) calendar days after the close of the calendar year or the fiscal year adopted by the QB. Report of such audit shall be submitted to the board of directors and the appropriate department of the SES not later than 120 calendar days after the close of the calendar year or the fiscal year adopted by the QB. The report to the BSP shall be accompanied by the:(1) certification by the external auditor on the: (a) dates of start and termination of audit; (b) date of submission of the FAR and certification under oath stating that no material weakness or breach in the internal control and risk management systems was noted in the course of the audit of the QB to the board of directors; and (c) the absence of any direct or indirect financial interest and other circumstances that may impair the independence of the external auditor; (2) reconciliation statement between the AFS and the balance sheet and IS for the QB and trust department submitted to the BSP including copies of adjusting entries on the reconciling items; and (3) other information that may be required by the BSP.

In addition, the external auditor shall be required by the QB to submit to the board of directors, a Letter of Comment (LOC) indicating any material weakness or breach in the institution's internal control and risk management systems within thirty (30) calendar days after submission of the FAR. If no material weakness or breach is noted to warrant the issuance of an LOC, a certification under oath stating that no material weakness or breach in the internal control and risk management systems was noted in the course of the audit of the QB shall be submitted in its stead, together with the FAR.

Material weakness shall be defined as a significant control deficiency, or combination of deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be detected or prevented by the institution's internal control. A material weakness does not mean that a material misstatement has occurred or will occur, but that it could occur. A control deficiency exists when the design or operation of a control does not

allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A *significant deficiency* is a control deficiency, or combination of control deficiencies, that adversely affects the institution's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles. The term *more than remote likelihood* shall mean that future events are likely to occur or are reasonably possible to occur.

The board of directors, in a regular or special meeting, shall consider and act on the FAR and the certification under oath submitted in lieu of the LOC and shall submit, within thirty (30) banking days after receipt of the reports, a copy of its resolution to the appropriate department of the SES. The resolution shall show, among other things, the actions(s) taken on the reports and the names of the directors present and absent.

The board shall likewise consider and act on the LOC and shall submit, within thirty (30) banking days after receipt thereof, a copy of its resolution together with said LOC to the appropriate department of the SES. The resolution shall show the action(s) taken on the findings and recommendations and the names of the directors present and absent, among other things.

The LOC shall be accompanied by the certification of the external auditor of the date of its submission to the board of directors.

Government-owned or -controlled banks, including their subsidiaries and affiliates, as well as other FIs under BSP supervision which are under the concurrent jurisdiction of the Commission on Audit (COA) shall be exempt from the aforementioned annual financial audit by an acceptable external auditor: *Provided,* That when warranted by supervisory concern such as material weakness/breach in internal control and/or risk management systems, the Monetary Board may, upon recommendation of the appropriate department of the SES, require the financial audit to be conducted by an external auditor acceptable to the BSP, at the expense of the QB*: Provided, further* , That when circumstances such as, but not limited to loans from multilateral FIs, privatization, or public listing warrant, the financial audit of the QB concerned by an acceptable external auditor may also be allowed.

QBs and other FIs under the concurrent jurisdiction of the BSP and COA shall, however, submit a copy of the annual audit report (AAR) of the COA to the appropriate department of the SES of the BSP within thirty (30) banking days after receipt of the report by the board of directors. The AAR shall be accompanied by the: (1) certification by the institution concerned on the date of receipt of the AAR by the board of directors; (2) reconciliation statement between the AFS in the AAR and the balance sheet and IS of the QB and trust department submitted to the BSP, including copies of adjusting entries on the reconciling items; and (3) other information that may be required by the BSP.

The board of directors of said institutions, in a regular or special meeting, shall consider and act on the AAR, as well as on the comments and observations and shall submit, within thirty (30) banking days after receipt of the report, a copy of its resolution to the appropriate department of the SES. The resolution shall show the action(s) taken on the report, including the comments and observations and the names of the directors present and absent, among other things.

The AFS required to be submitted shall in all respect be PFRS/PAS compliant: *Provided,* That FIs shall submit to the BSP

adjusting entries reconciling the balances in the financial statements for prudential reporting with that in the audited annual financial statements.

QBs as well as external auditors shall strictly observe the requirements in the submission of the FAR and reports required to be submitted under *Appendix Q-33*.

The reports and certifications of QBs, schedules and attachments required under this Subsec. shall be considered Category *B* reports, delayed submission of which shall be subject to the penalties under Subsec. 4192.Q.3.b.II.

(As amended by Circular Nos. 554 dated 22 December 2006 and 540 dated 09 August 2006)

§ 4190Q.1 ***(Reserved)***

§ 4190Q.2 ***(2008 - 4172Q.1) Posting of audited financial statements.*** QBs shall post in conspicuous places in their head offices, all their branches and other offices, as well as in their respective web-sites, their latest FAR.

(As amended by Circular No. 540 dated 9 August 2006)

§ 4190Q.3 ***(2008 - 4172Q.2) Disclosure of external auditor's adverse findings to the Bangko Sentral; sanction***

a. *Findings to be disclosed.* QBs shall require their external auditors to report to the BSP any matter adversely affecting the condition or soundness of the bank, such as, but not limited to:

(1) Any serious irregularity, including those involving fraud or dishonesty, that may jeopardize the interest of creditors;

(2) Losses incurred which substantially reduce the capital funds of the QB; and

(3) Inability of the auditor to confirm that the claims of creditors are still covered by the QB's assets.

The disclosure of information by the external auditor to the BSP shall not be a ground for civil, criminal or disciplinary proceedings against the former.

QB management shall be present during discussions or at least be informed of the adverse findings in order to preserve the concerns of the supervisory authority and external auditors regarding the confidentiality of information.

b. *Sanction*. The auditing firm(s) shall be blacklisted by the Monetary Board for a period as the Board may deem appropriate for their failure to perform their duty of reporting to the BSP any matter adversely affecting the condition or soundness of the QB. QBs shall not be allowed to engage the services of the blacklisted auditing firm.

§ 4190Q.4 ***(2008 - 4172Q.3) Disclosure requirement in the notes to the audited financial statements***. QBs shall require their external auditors to include the following additional information in the notes to financial statements:

a. Basic quantitative indicators of financial performance such as return on average equity, return on average assets and net interest margin;

b. Capital-to-risk assets ratio under Sec. 4115Q;

c. Concentration of credit as to industry/economic sector where concentration is said to exist when total loan exposures to a particular industry/ economic sector exceeds thirty percent (30%) of total loan portfolio (TLP);

d. Breakdown of total loans as to secured and unsecured and breakdown of secured loans as to type of security;

e. Total outstanding loans to QB's DOSRI, percent of DOSRI loans to total loan portfolio, percent of unsecured DOSRI loans to total DOSRI loans, percent of past due DOSRI loans to total DOSRI loans and percent of non-performing DOSRI loans to total DOSRI loans;

f. Nature and amount of contingencies and commitments arising from off-balance sheet items [include direct

credit substitutes (e.g., export Letter of Credit (LCs) confirmed, underwritten accounts unsold), transaction-related contingencies (e.g., performance bonds, bid bonds, standby LCs), short-term self-liquidating trade related contingencies arising from the movement of goods (e.g., sight/usance domestic LCs, sight/usance import LCs), sale and repo agreements not recognized in the balance sheet; interest and FX rate related items; and other commitments];

g. Provisions and allowances for losses and how these are determined;

h. Aggregate amount of secured liabilities and assets pledged as security; and

i. Accounting policies which shall include, but shall not be limited to, general accounting principles, changes in accounting policies/practices, principles of consolidation, policies and methods for determining when assets are impaired, recognizing income on impaired assets and losses on non-performing credits, income recognition, valuation policies and accounting policies on securitizations, foreign currency translations, loan fees, premiums and discounts, repo agreements, premises/fixed assets, income taxes, derivatives, etc.

For purposes of computing the indicators in Item *"a"* above, the following formulas shall be used:

a. Return on Average Equity (%) = $\dfrac{\textbf{Net Income (or Loss) after Income Tax x 100}}{\textbf{Average Total Capital Accounts}}$

Where:

Average Total Capital Accounts = $\dfrac{\text{Sum of Total Capital Accounts as of the 12 month-ends in the calendar/fiscal year adopted by the QB}}{12}$

b. Return on Average Assets (%) = $\dfrac{\textbf{Net Income (or Loss) after Income Tax x 100}}{\textbf{Average Total Assets}}$

Where:

Average Total Assets = $\dfrac{\text{Sum of Total Assets as of the 12 month-ends in the calendar/fiscal year adopted by the QB}}{12}$

c. Net Interest Margin (%) = $\dfrac{\textbf{Net Interest Income x 100}}{\textbf{Average Interest Earning Assets}}$

Where:

Net Interest Income Expense = Total Interest Income – Total Interest

Average Interest Earning Assets = $\dfrac{\text{Sum of Total Interest Earning Assets as of the 12 month-ends in the calendar/fiscal year adopted by the QB}}{12}$

§ 4190Q.5 ***(2008 - 4172Q.4) Disclosure requirements in the annual report.*** QBs shall prepare an annual report which shall include, in addition to the AFS and other usual information contained therein, a discussion and/or analysis of the following information:

a. Financial performance;

b. Financial position and changes therein;

c. Overall risk management philosophy (a general statement of the risk management policy adopted by the QB's board of directors which serves as the basis for the establishment of its risk management system), risk management system and structure;

d. Qualitative and quantitative information on risk exposures (credit, market, liquidity, operational, legal and other risks); and

e. Basic business management and corporate governance information such as the QB's organizational structure, incentive structure including its remuneration policies, nature and extent of transactions with affiliates and related parties.

§ 4190Q.6 ***(2008 - 4172Q.5) Posting and submission of annual report.*** A copy of the latest annual report shall be posted by the QB in a conspicuous place in its head office, all its branches and other offices.

The deadline for the submission of the annual report to the appropriate department of the SES is 180 calendar days after the close of the calendar or fiscal year adopted by the QB.

Sec. 4191Q *(2008 - 4161Q)* Records. QBs shall have a true and accurate account, record or statement of their daily transactions. The making of any false entry or the willful omission of entries relevant to any transaction is a ground for the imposition of administrative sanctions under Section 37 of R.A. No. 7653, without prejudice to the criminal liability of the director or officer responsible therefor under Sections 35 and 36 of R.A. No. 7653 and/or the applicable provisions of the Revised Penal Code. Records shall be up-to-date and shall contain sufficient detail so that an audit trail is established.

§ 4191Q.1 *(2008 - 4161Q.1) Uniform system of accounts*. QBs shall strictly adopt/implement the Uniform System of Accounts prescribed for QBs in the recording of daily transactions including reportorial and publication requirements.

§ 4191Q.2 *(Reserved)*

§ 4191Q.3 *(2008 - 4161Q.2) Philippine Financial Reporting Standards/Philippine Accounting Standards*

Statement of policy. It is the policy of the BSP to promote fairness, transparency and accuracy in financial reporting. It is in this light that the BSP aims to adopt all PFRS and PAS issued by the Accounting Standards Council (ASC) to the greatest extent possible.

QBs/FIs shall adopt the PFRS and PAS which are in accordance with generally accepted accounting principles in recording transactions and in the preparation of financial statements and reports to BSP. However, in cases where there are differences between BSP regulations and PFRS/PAS as when more than one (1) option are allowed or certain maximum or minimum limits are prescribed by the PFRS/PAS, the option or limit prescribed by BSP regulations shall be adopted by FIs.

For purposes hereof, the PFRS/PAS shall refer to issuances of the ASC and approved by the PRC.

Accounting treatment for prudential reporting. For prudential reporting, FIs shall adopt in all respect the PFRS and PAS except as follows:

a. In preparing consolidated financial statements, only investments in financial allied subsidiaries except insurance subsidiaries shall be consolidated on a line-by-line basis; while insurance and non-financial allied subsidiaries shall be accounted for using the equity method. Financial/non-financial allied/non-allied associates shall be accounted for using the equity method in accordance with the provisions of PAS 28 "Investments in Associates".

b. For purposes of preparing separate financial statements, financial/non-financial allied/non-allied subsidiaries/associates, including insurance subsidiaries/associates, shall also be accounted for using the equity method; and

c. FIs shall be required to meet the BSP recommended valuation reserves.

Government grants extended in the form of loans bearing nil or low interest rates shall be measured upon initial recognition at its fair value (i.e., the present value of the future cash flows of the financial instrument discounted using the market interest rate). The difference between the fair value and the net proceeds of the loan shall be recorded under "*Unearned Income-Others*", which shall be amortized over the term of the loan using the effective interest method.

The provisions on government grants shall be applied retroactively to all outstanding government grants received. FIs that adopted an accounting treatment other than the foregoing shall consider the adjustment as a change in accounting policy, which shall be accounted for in accordance with PAS 8.

Notwithstanding the exceptions in Items *"a", "b" and "c",* the audited annual financial statements required to be submitted to the BSP in accordance with the provision of Sec. 4190Q shall in all respect be PFRS/PAS compliant: *Provided,* That FIs shall submit to the BSP adjusting entries reconciling the balances in the financial statements for prudential reporting with that in the audited annual financial statements.

(As amended by Circular No. 572 dated 22 June 2007)

Sec. 4192Q *(2008 - 4162Q/4162Q.2)* **Reports/Manner of filing.** QBs shall submit to the appropriate department of the SES the reports listed in *Appendix Q-3* in the forms as may be prescribed by the Deputy Governor, SES.

Any change in, or amendment to, the articles of incorporation, by-laws or material documents required to be submitted to the BSP shall be reported by submitting copies of the amended articles of incorporation, by laws, or material documents to the appropriate department of the SES within fifteen (15) days following such change.

In the case of the independent directors, the bio-data shall be accompanied by a *certification under oath* from the director concerned that he/she is an independent director as defined under Subsec. 4141Q.1 that all the information thereby supplied are true and correct, and that he/she:

1. Is not or has not been an officer or employee of the QB/trust entity, its subsidiaries or affiliates or related interests during the past three (3) years counted from the date of his/her election;

2. Is not a director or officer of the related companies of the institution's majority stockholder;

3. Is not a majority stockholder of the institution, any of its related companies, or of its majority shareholders;

4. Is not a relative within the fourth degree of consanguinity or affinity, legitimate or common-law of any director, officer or majority shareholder of the QB/trust entity or any of its related companies;

5. Is not acting as a nominee or representative of any director or substantial shareholder of the QB/trust entity, any of its related companies or any of its substantial shareholders;

6. Is not retained as professional adviser, consultant, agent or counsel of the institution, any of its related companies or any of its substantial shareholders, either in his/her personal capacity or through his/her firm; is independent of management and free from any business or other relationship, has not engaged and does not engage in any transaction with the institution or with any of its related companies or with any of its substantial shareholders, whether by himself/herself or with other persons or through a firm of which he/she is a partner or a company of which he/she is a director or substantial shareholder, other than transactions which are conducted at arms length and could not materially interfere with or influence the exercise of his/her judgment; and

7. Complies with all the qualifications required of an independent director and does not possess any of the disqualifications therefor and has not withheld nor suppressed any information material to his/her qualification or disqualification as an independent director.

The submission of the reports shall be effected by filing them personally with the appropriate department of the SES or with the BSP Regional Offices/Units, or by sending them by registered mail or special delivery through private couriers unless otherwise specified in the circular or memorandum of the BSP.

Where the reports are prescribed by the BSP to be submitted through

electronic mail, the original notarized affidavit/last page of each report, hard copy of the covering control prooflist, or any other related documents required to be submitted shall be filed in the manner prescribed in the preceding paragraph.

In line with the policy direction of R.A. No. 8792 (E-Commerce Act), the BSP is strongly encouraging QBs to submit their regular reports to the BSP in electronic form.

However, the BSP cannot presently guarantee the security/confidentiality of data in the course of transmitting electronic reports to BSP. BSP recommends that sensitive or confidential information be provided by ordinary post or courier. The BSP will accept no responsibility for electronic messages/ reports/information that may be hacked or cracked, intercepted, copied or disclosed outside BSP's information system.

(As amended by Circular Nos. 591 dated 27 December 2007, CL-2007-059 dated 28 November 2007, CL-2007-050 dated 04 October 2007, 576 dated 08 August 2007, 574 dated 10 July 2007, 560 dated 31 January 2007, and 557 dated 12 January 2007)

§ 4192Q.1 ***(2008 - 4162Q.1) Categories and signatories of reports.*** Reports required to be submitted to the BSP are classified into Categories A-1, A-2, A-3 and B reports as indicated in the list of reports required to be submitted to the BSP in *Appendix Q-3*.

Appendix Q-4 prescribes the signatories for each report category and the requirements on signatory authorization.

Reports submitted by QBs in computer media shall be subject to the same requirements.

A report submitted to the BSP under the signature of an officer who is not authorized in accordance with the requirements in this Subsection shall be considered as not having been submitted.

§ 4192Q.2 ***(2008 - 4162Q.3) Sanctions in case of willful delay in the submission of reports/refusal to permit examination***

a. *Definition of terms*. For purposes of this Subsection, the following definitions shall apply:

(1) *Report* shall refer to any report or statement required of a QB to be submitted to the BSP periodically or within a specified period.

(2) *Willful delay in the submission of reports* shall refer to the failure of a QB to submit a report on time. Failure to submit a report on time due to fortuitous events, such as fire and other natural calamities and public disorders, including strike or lockout affecting a QB as defined in the Labor Code or national emergency affecting operations of QBs, shall not be considered as willful delay.

(3) *Examination* shall include, but need not be limited to, the verification, review, audit, investigation and inspection of the books and records, business affairs, administration and financial condition of any QB including the reproduction of its records, as well as the taking possession of the books and records and keeping them under the BSP's custody after giving proper receipt therefore. It shall also include the interview of the directors and personnel of the QB including its EDP servicer. Books and records shall include, but shall not be limited to, data and information stored in magnetic tapes, disks, printouts, logbooks and manuals kept and maintained by the QB or the EDP servicer, necessary and incidental to the use of EDP systems by the QB.

(4) *Refusal to permit examination* shall mean any act or omission which impedes, delays, or obstructs the duly authorized BSP officer/examiner/employee from conducting an examination, including the act of refusing to accept or honor a letter of authority to examine presented by any officer/examiner/employee of the BSP.

b. *Fines for willful delay in submission of reports*. QBs incurring willful delay in the submission of required reports shall pay a fine in accordance with the following schedule:

I. *For Categories A-1, A-2 and A-3 reports*	
Per day of default until the report is filed	₱600
II. *For Category B reports*	
Per day of default until the report is filed	₱120

Delay or default shall start to run on the day following the last day required for the submission of reports. However, should the last day of filing fall on a non-working day in the locality where the reporting FI is situated, delay or default shall start to run on the day following the next working day. The due date/deadline for submission of reports to BSP as prescribed under Sec. 4192Q governing the frequency and deadlines indicated in *Appendix Q-3* shall be automatically moved to the next business day whenever a halfday suspension of business operations in government offices is declared due to an emergency such as typhoon, floods, etc.

For purposes of establishing delay or default, the date of acknowledgment by the appropriate department of the SES or the BSP Regional Offices/Units appearing on the copies of such reports filed or submitted, the date of mailing postmarked on the envelope/the date of registry/ special delivery receipt, as the case may be, or the date of the acknowledgment receipt issued by the appropriate office of the BSP if the reports were submitted through electronic mail, shall be considered as the date of filing by the QB.

Delayed schedules/attachments and amendments shall be considered late reporting subject to the above penalties.

c. *Fines for refusal to permit examination*

(1) *Amount of fine* - Any QB which shall willfully refuse to permit examination shall pay a fine of P3,000 daily from the day of refusal and for as long as such refusal lasts.

(2) *Procedures in imposing the fine* -

(a) The BSP officer/examiner/employee shall report the refusal of the QB to permit examination to the head of the appropriate department of the SES, who shall forthwith make a written demand upon the concerned for such examination. If the QB continues to refuse said examination without any satisfactory explanation therefore, the BSP officer/examiner/employee concerned shall submit a report to that effect to the said department head.

(b) The fine shall be imposed starting on the day following the receipt by the said department of the written report submitted by the BSP officer/examiner/employee concerned regarding the continued refusal of the QB to permit the desired examination.

d. *Manner of payment or collection of fines* - The regulations embodied in Sec. 4902Q shall be observed in the collection of the fines from QBs.

e. *Other penalties* - The imposition of the foregoing penalties shall be without prejudice to the imposition of the other administrative sanctions and to the filing of a criminal case as provided for in other provisions of law.

f. *Appeal to the Monetary Board* -

Any aggrieved QB may appeal to the Monetary Board a ruling of the appropriate department of the SES imposing a fine.

(As amended by Circular No. 585 dated 15 October 2007)

§ 4192Q.3 ***(2008 - 4181Q) Publication requirements.*** The quarterly CSOC of a QB/ trust entity and its subsidiaries and associates shall be published side-by-side with the SOC of its head office and its branches/other offices as of such dates as the BSP may require, within twenty (20)

working days from receipt of call letter, in any newspaper of general circulation in the country in the prescribed format.

The CSOC of a QB/trust entity and its subsidiaries and associates shall conform with the guidelines of PAS 27 "Consolidated and Separate Financial Statements", except that for purposes of consolidated financial statements, only investments in financial allied subsidiaries except insurance subsidiaries shall be consolidated on a line-by-line basis; while insurance and non-financial allied subsidiaries shall be accounted for using the equity method. Financial/non-financial allied/non-allied associates shall be accounted for using the equity method in accordance with the provisions of PAS 28 "Investments in Associates". For purposes of separate financial statements, investments in financial/non-financial allied/non-allied subsidiaries/associates, including insurance subsidiaries/ associates, shall be accounted for using the equity method.

a. The following information shall be disclosed in the Statements of Condition:

(1) Non-performing loans (NPLs) and ratio to total loan portfolio;

(2) Classified loans and other risk assets;

(3) General loan loss reserve;

(4) Specific loan loss reserve;

(5) Return on equity (ROE);

(6) DOSRI loans/advances and ratio to total loan portfolio; and

(7) Past due DOSRI loans/advances and ratio to total loan portfolio.

For uniform calculation of the additional information required, the guidelines in Annex Q-3-f of *Appendix Q-3* shall be observed.

b. The names and positions/ designations of:

(1) members of the board of directors; and

(2) president and executive vice-presidents (senior vice-presidents, if there are no executive vice-president) or equivalent positions shall be presented in the right side column of the published SOC as of June of every year.

O. PROMPT CORRECTIVE ACTION FRAMEWORK

Sec. 4193Q *(2008 - 4192Q)* Prompt Corrective Action Framework. The framework for the enforcement of prompt corrective action (PCA) on banks which is in *Appendix Q-40,* shall govern the PCA taken on QBs to the extent applicable, or by analogy.

(Circular No. 523 dated 23 March 2006, as amended by Circular No. 664 dated 15 September 2009)

Sec. 4194Q (Reserved)

P. (RESERVED)

Secs. 4195Q - 4198Q (Reserved)

Q. GENERAL PROVISION ON SANCTIONS

Sec. 4199Q General Provision on Sanctions. Any violation of the provisions of this Part shall be subject to Sections 36 and 37 of R.A. No. 7653.

The guidelines for the imposition of monetary penalty for violations/offenses with sanctions falling under Section 37 of R. A. No. 7653 on QBs, their directors and/or officers are shown in *Appendix Q-39*.

PART TWO

DEPOSIT SUBSTITUTES AND BORROWING OPERATIONS

A. - D. (RESERVED)

Secs. 4201Q - 4234Q (Reserved)

E. DEPOSIT SUBSTITUTE OPERATIONS

Section 4235Q *(2008 - 4211Q)* Deposit Substitute Instruments. Only the following types of instruments may be issued by QBs as evidence of deposit substitute liabilities:

a. Promissory notes;

b. Repurchase agreements (Repos); and

c. Certificates of assignment/ participation with recourse.

§ 4235Q.1 *(2008 - 4211Q.1) Prohibition against use of certain instruments as deposit substitutes.* Acceptances, bills of exchange and trust certificates shall not be used as evidence of deposit substitute liabilities. This prohibition shall not apply to the acceptance or negotiation of bills of exchange in connection with trade transactions, or to the issuance of trust certificates creating trust relationship.

§ 4235Q.2 *(2008 - 4211Q.2) Negotiations of promissory notes.* Negotiable promissory notes acquired by QBs shall not be negotiated by mere indorsement and/or delivery, if they do not conform with the minimum features prescribed under Subsec. 4235Q.3. If these notes do not contain the features in said Subsection, their negotiation shall be covered by any of the appropriate deposit substitute instruments mentioned in Sec. 4235Q.

§ 4235Q.3 *(2008 - 4211Q.3) Minimum features.* Deposit substitute instruments issued by QBs shall have the following minimum features.

a. The present value and maturity value and/or the principal amount and interest rate and such other information as may be necessary to enable the parties to determine the cost or yield of the borrowing or placement shall be specified.

b. The date of issuance shall be indicated at the upper right corner of the instrument, and directly below which shall be the maturity period or the word "demand", if it is a demand instrument.

c. The payee may be identified by his trust account/deposit account number in both negotiable and non-negotiable instruments.

d. Securities which are the subject of a repo or a certificate of assignment/ participation with recourse, shall be particularly described on the face of said instruments or on a separate instrument attached and specifically referred to therein and made an integral part thereof as to the maker, value, maturity, serial number, and such other particulars as shall clearly identify the securities.

e. The instrument shall provide for the payment of liquidated damages, in addition to stipulated interest, in case of default by the maker/issuer, as well as attorney's fees and cost of collection in case of suit.

f. A conspicuous notice at the lower center margin of the face of the instrument that the transaction is not insured by the PDIC.

g. The corporate name of the issuer shall be printed at the upper center margin of the instrument and directly below which shall be a designation of the instrument, such as, "Promissory Note" or "Repo".

h. The words "duly authorized officer" shall be placed directly below the signature of the person signing for the maker/issuer.

i. Each instrument shall be serially pre-numbered.

j. The copy delivered to the payee shall bear the word "Original" and the copies retained by the issuer shall be identified as "Duplicate," "File Copy" or words of similar import.

k. Only security paper with adequate safeguards against alteration or falsification shall be used.

Deposit substitute instruments shall conform to the language prescribed by the BSP.

Any substantial deviation therefrom or any additional stipulation therein shall be referred to the BSP for prior approval. The size and appearance of these instruments shall not be similar to the size and appearance of checks. Formats of standardized instruments in *Appendices Q-6 to Q-6-k* shall be followed.

Rubber stamping, typewriting and handwriting some provision shall not be considered compliance with said regulations.

Borrowings of QBs from the loans and discounts window of banks or QBs shall be exempted from the documentation requirements of this Section: *Provided,* That the exemption from the documentation requirements shall not be construed or interpreted as exemption of said borrowings from the other rules on borrowings by QBs and from other BSP regulations on deposit substitutes.

§ 4235Q.4 ***(2008 - 4211Q.7)Interbank borrowings.*** Except for interbank borrowings which are settled through the QB's respective DDAs with the BSP via PhilPaSS, all interbank borrowings shall be evidenced by deposit substitute instrument containing the minimum features prescribed in Subsec. 4235Q.3 .

(As amended by Circular No, 703 dated 23 December 2010)

§ 4235Q.5 ***(2008 - 4211Q.4) Delivery of securities***[1]

a. Securities, warehouse receipts, quedans and other documents of title which are the subject of quasi-banking functions, such as repos, shall be physically delivered, if certificated, to a BSP accredited custodian that is mutually acceptable to the lender/purchaser and borrower/seller, or by means of book-entry transfer to the appropriate securities account of the BSP accredited custodian in a registry for said securities, if immobilized or dematerialized while the overlying principal borrowing instrument shall be physically delivered to the lender/purchaser. The custodian shall hold the securities in the name of the borrower/seller, but shall keep said securities segregated from the regular securities account of the borrower/seller if the borrower/seller has an existing securities account with the custodian. *Provided,* That a financial institution (NBFI) authorized by the BSP to perform custodianship function may not be allowed to be custodian of securities issued or owned by said institution, its subsidiaries or affiliates, or of securities in bearer form.

The delivery shall be effected upon payment and shall be evidenced by a securities delivery receipt duly signed by authorized officers of the custodian and delivered to both the lender/purchaser and seller/borrower.

Sanctions. Violation of any provision of Item *"a"* shall be subject to the following sanctions/penalties:

(1) *Monetary penalties*

First Offense – Fine of P10,000 a day for each violation reckoned from the date the violation was committed up to the date it was corrected.

Subsequent offenses – Fine of P20,000 a day for each violation reckoned from the date the violation was committed up to the

[1] Effective 16 November 2004 under Circular No. 450 dated 06 September 2004.

date it was corrected.

(2) *Other sanctions*

First offense – Reprimand for the directors/officers responsible for the violation.

Subsequent offense –

(a) Suspension for ninety (90) days without pay of directors/officers responsible for the violation;

(b) Suspension or revocation of the accreditation to perform custodianship function;

(c) Suspension or revocation of the authority to engage in quasi-banking function; and/or

(d) Suspension or revocation of the authority to engage in trust and other fiduciary business.

b. The guidelines to implement the delivery by the seller of securities to the buyer or to his designated third party custodian are shown in *Appendix Q-38*.

Sanctions. Without prejudice to the penal and administrative sanctions provided for under Sections 36 and 37, respectively of the R.A. No. 7653 (The New Central Bank Act), violation of any provision of the guidelines in *Appendix Q-38* shall be subject to the following sanctions/penalties depending on the gravity of the offense:

(a) *First offense* –

(1) Fine of up to P10,000 a day or the institution for each violation reckoned from the date the violation was committed up to the date it was corrected; and

(2) Reprimand for the directors/officers responsible for the violation.

(b) *Second offense* -

(1) Fine of up to P20,000 a day for the institution for each violation reckoned from the date the violation was committed up to the date it was corrected; and

(2) Suspension for ninety (90) days without pay of directors/officers responsible for the violation.

(c) *Subsequent offenses*–

(1) Fine of up to P30,000 a day for the institution for each violation from the date the violation was committed up to the date it was corrected;

(2) Suspension or revocation of the authority to act as securities custodian and/or registry; and

(3) Suspension for 120 days without pay of the directors/officers responsible for the violation.

(As amended by M-2007-002 dated 23 January 2007; M-2006-009 dated 06 July 2006, M-2006-002 dated 05 June 2006 and Circular No. 524 dated 31 March 2006)

§ 4235Q.6 *(2008 - 4211Q.5) Other rules and regulations governing the issuance and treatment of deposit substitute instruments*

a. If there is any stipulation that payment of the deposit substitute shall be chargeable against a particular deposit account of the maker or issuer that is maintained with another bank, it shall further provide that the liability of the maker or issuer of the instrument shall not be limited to the outstanding balance of said deposit account.

b. Any agreement allowing the issuer or maker to substitute the underlying securities shall further provide that the actual substitution shall be with the prior written consent of the payee.

c. Automatic renewal upon maturity of the instrument may be effected only under terms and conditions previously stipulated by the parties.

d. Stipulations between the maker or issuer and the payee which are embodied in separate instruments shall be specifically referred to in the deposit substitute instruments and made an integral part thereof.

e. In the case of repurchase agreements and certificates of assignment/participation with recourse, the stipulation shall clearly state either (a) that the underlying securities are being delivered to the buyer or assignee

as collaterals or (b) that the ownership thereof is being transferred to the buyer or assignee.

f. The regulations on interbank loan transactions prescribed in Sec. 4343Q shall also apply to interbank borrowings.
(As amended by Circular No, 703 dated 23 December 2010)

§ 4235Q.7 ***(2008 - 4211Q.6) Substitution of underlying securities***
(Deleted by Circular No. 703 dated 23 December 2010)

§ 4235Q.8 ***(2008 - 4211Q.7) Call slips/ tickets for 24-hour loans***
(Renumbered by Circular No. 703 dated 23 December 2010)

§ 4235Q.9 ***(2008 - 4211Q.8) Requirement to state nature of underlying securities***
(Deleted by Circular No. 703 dated 23 December 2010)

§ 4235Q.10 ***(2008 - 4211Q.9) Compliance with SEC rules.*** QBs shall comply with the new rules on the registration of short-term and long-term commercial papers appended hereto as *Appendices Q-7 and Q-8*.

§ 4235Q.11 ***(Reserved)***

§ 4235Q.12 ***(2008 - 4211Q.12) Repurchase agreements covering government securities, commercial papers and other negotiable and non-negotiable securities or instruments.*** The following regulations shall govern REPOs covering government securities, commercial papers and other negotiable and non-negotiable securities or instruments of QBs as well as sale on a without recourse basis of said securities by QBs.

a. *Proper recording and documentation of repos.*

QBs shall have a true and accurate account, record or statement of their daily transactions. As such, repos covering government securities, commercial papers and other negotiable and non-negotiable securities or instruments must be properly recorded and documented in accordance with existing BSP regulations.

The absence of proper documentation for repos is tantamount to willful omission of entries relevant to any transaction, which shall be a ground for the imposition of administrative sanctions and the disqualification from office of any director or officer responsible therefor under existing laws and regulations.

b. *Responsibilities of the chief executive officer (CEO) or officer of equivalent rank.*

It shall be the responsibility of the CEO or the officer of equivalent rank in a QB to:

(1) Institute policies and procedures to prevent undocumented or improperly documented repos covering government securities, commercial papers and other negotiable and non-negotiable securities or instruments;

(2) Submit a notarized certification at the end of every semester that the QB did not enter into any repo covering government securities, commercial papers and other negotiable and non-negotiable securities or instruments that are not documented in accordance with existing BSP regulations and that the QB has strictly complied with the pertinent rules of the SEC and the BSP on the proper sale of securities to the public and performed the necessary representations and disclosures on the securities particularly the following:

(a) Informed the clients that such securities are not deposits and as such, do not benefit from any insurance otherwise applicable to deposits such as, but not limited to, R.A. No. 3591, as amended, otherwise known as the PDIC law;

(b) Informed and explained to the client all the basic features of the security

being sold on a without recourse basis, such as but not limited to:

(i) issuer and its financial condition;

(ii) term and maturity date;

(iii) applicable interest rate and its computation;

(iv) tax features (whether taxable, tax paid or tax-exempt);

(v) risk factors and investment considerations;

(vi) liquidity feature of the instrument:

(aa) procedures for selling the security in the secondary market (e.g., OTC or exchange);

(bb) authorized selling agents; and

(cc) minimum selling lots.

(vii) disposition of the security:

(aa) registry (address and contact numbers);

(bb) functions of the registry; and

(cc) pertinent registry rules and procedures.

(viii) collecting and paying agent of the interest and principal; and

(ix) other pertinent terms and conditions of the security and if possible, a copy of the prospectus or information sheet of the security.

(c) Informed the client that pursuant to Subsecs. 4235Q.5 and 4101Q.4:

(i) Securities sold under repos shall be physically delivered, if certificated, to a BSP accredited custodian that is mutually acceptable to the client and the QB, or by means of book-entry transfer to the appropriate securities account of the BSP accredited custodian in a registry for said securities, if immobilized or dematerialized; and

(ii) Securities sold on a without recourse basis are required to be delivered physically to the purchaser, or to his designated custodian duly accredited by the BSP, if certificated, or by means of book-entry transfer to the appropriate securities account of the purchaser or his designated custodian in a registry for said securities if immobilized or dematerialized.

(d) Clearly stated to the client that:

(i) The QB does not guarantee the payment of the security sold on a "without recourse basis" and in the event of default by the issuer, the sole credit risk shall be borne by the client; and

(ii) The QB is not performing any advisory or fiduciary function.

(3) Report to the appropriate department of the SES any undocumented repo within seventy-two (72) hours from knowledge of such transactions.

c. *Treatment as deposit substitutes* All sales of government securities, commercial papers and other negotiable and non-negotiable securities or instruments that are not documented in accordance with existing BSP regulations shall be deemed to be deposit substitutes subject to regular reserves.

d. *Certification*. The submission deadline for the required certification from the CEO/officer of equivalent rank of the QB shall initially be 1 February 2005 using the format in *Appendix Q-36-a*. Thereafter, the required succeeding certification shall be submitted within five (5) banking days from end of reference semester using the format in *Appendix Q-36*.

e. *Sanctions*. The Monetary Board may, at its evaluation and discretion, impose any or all of the following sanctions to a QB or the director/s or officer/s found to be responsible for repos covering government securities, commercial papers and other negotiable and non-negotiable securities or instruments that are not documented in accordance with existing BSP regulations:

(1) Fine of up to P30,000 a day to the concerned entity for each violation from the date the violation was committed up to the date it was corrected;

(2) Suspension of interbank clearing privileges/immediate exclusion from

clearing;

(3) Suspension of access to BSP rediscounting facilities;

(4) Suspension of lending or foreign exchange operations or authority to accept new deposits or make new investments;

(5) Revocation of quasi-banking license;

(6) Revocation of authority to perform trust operations; and

(7) Suspension for 120 days without pay of the directors/officers responsible for the violation.

§ 4235Q.13 ***(2008 - 4212Q) Recording; payment; maturity; renewal***

(Deleted by Circular No. 703 dated 12 December 2010)

§ 4235Q.14 ***(2008 - 4214Q) Interbank borrowings***

(Deleted by Circular No. 703 dated 23 December 2010)

§ 4235Q.15 ***(2008 - 4215Q) Borrowings from trust departments or managed funds of banks or investment houses.*** Funds borrowed by QBs from trust departments or managed funds of banks or IHs are not considered as interbank borrowings and, therefore, are subject to the:

a. reserve requirement on deposit substitutes; and

b. minimum trading lot rule.

(As amended by Circular No. 703 dated 23 December 2010)

Sec. 4236Q ***(2008 - 4213Q)*** **Minimum Trading Lot.** The minimum size of any single deposit substitute transaction shall be P50,000.

In connection with the minimum trading lot rule above stated, no QB shall issue deposit substitute instruments in the name of two (2) or more persons or accounts except those falling under the following relationships in which cases, commingling may be allowed: (a) husband and wife; (b) persons related to each other within the second degree of consanguinity; and (c) in trust for (ITF) arrangements.

Sec. 4237Q ***(2008 - 4216Q)*** **Money Market Placements of Rural Banks.** QBs shall not accept money market placements from any RB unless the latter presents a certification under oath stating: (a) that it has no overdue special time deposits; (b) that it has no past due obligations with the BSP or other government FIs; (c) the amount of its current obligations, if any, with said government FIs; and (d) the amount of its total outstanding money market placements. However, in no case shall such QBs sell receivables to RBs without recourse.

§ 4237Q.1 ***(2008 - 4216Q.1) Definition of terms.*** As used in this Section, the following terms shall have the following meanings:

Money market placements shall include investments in debt instruments, including purchases of receivables with recourse to the lending institution, except purchases of government securities on an outright basis.

Government securities shall include evidences of indebtedness of the Republic of the Philippines and the BSP and other evidences of indebtedness or obligations of government entities, the servicing and repayment of which are fully guaranteed by the Republic of the Philippines.

§ 4237Q.2 ***(2008 - 4216Q.2) Conditions required on accepted placements*** Placements accepted must comply with the following conditions:

a. That the total money market placements of an RB, as stated in the certification, including the placement being accepted by the entity concerned, shall not exceed the RB's combined capital accounts or net worth less current obligations with the BSP or other government FIs;

b. The maturity of the money market placement shall not exceed sixty (60) days; and

c. That placements shall be evidenced in all cases by promissory notes of accepting entities/REPOs and/or certificates of participation/assignment with recourse and that underlying instruments shall be government securities the servicing and repayment of which are guaranteed by the Republic of the Philippines.

§ 4237Q.3 ***(2008 - 4216Q.3) Sanctions*** Violations of the provisions of this Section shall be subject to the following sanctions/penalties:

a. *Fines*

First offense - Fines of P3,000 a day, reckoned from the date placement started up to the date when said placement was withdrawn, for each violation shall be assessed on the bank.

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Subsequent offenses - Fines of P5,000 a day, reckoned from the date placement started up to the date placement was withdrawn, for each violation shall be assessed on the bank.

b. *Other sanctions*

First offense - Reprimand for the directors/officers who approved the acceptance/placement with a warning that subsequent violations will be subject to more severe sanctions.

Subsequent offenses -

(1) Suspension for ninety (90) days without pay for directors/officers who approved the placement.

(2) Suspension or revocation of the authority to engage in quasi-banking functions.

Sec. 4238Q *(2008 - 4391Q.2)* Without Recourse Transactions. No QB shall sell, discount, assign, negotiate, in whole or in part such as thru syndications, participations and other similar arrangements, any note, receivable, loan, debt instrument and any type of financial asset or claim, except government securities, on a without recourse basis, or be a party in any capacity in any such transactions on a without recourse basis, unless such receivable, note, loan, debt instrument and financial asset or claim is registered with the SEC. This prohibition includes transactions between an investment house and its trust department.

Sec. 4239Q *(2008 - 4217Q)* Bond Issues of Quasi-banks. The following guidelines shall govern the bond issues of QBs.

§ 4239Q.1 *(2008 - 4217Q.1) Definition of terms.* For purposes of this Section, the following terms shall mean:

a. *Government securities* shall refer to the evidences of indebtedness of the Republic of the Philippines or its instrumentalities, or of the BSP, and must be freely negotiable and regularly serviced.

b. *Net book value* shall refer to the acquisition cost of property or accounts, plus additions and improvements thereon, less valuation reserves, if any.

c. *Current market value* shall refer to the value of the property as established by a duly licensed and independent appraiser.

d. *Affiliate* shall refer to an entity linked directly or indirectly to a QB by means of:

(1) Ownership, control or power to vote, of ten percent (10%) or more of the outstanding voting stocks of the entity, or vice-versa;

(2) Interlocking directorships or officerships;

(3) Common stockholders owning ten percent (10%) or more of the outstanding voting securities;

(4) Management contract or any arrangement granting power to direct or cause the direction of management and policies;

(5) Voting trustee holding ten percent (10%) or more of the outstanding voting securities;

(6) Permanent proxy or voting trust constituting ten percent (10%) or more of the outstanding voting securities.

e. *Subsidiary* shall refer to a corporation or firm more than fifty percent (50%) of the outstanding voting stock of which is directly or indirectly owned, controlled, or held with power to vote by another.

§ 4239Q.2 *(2008 - 4217Q.3) Compliance with SEC rules.* QBs issuing or intending to issue bonds shall comply with the new rules on the registration of long-term commercial papers *(Appendix Q-8)*.

§ 4239Q.3 *(2008 - 4217Q.4) Notice to Bangko Sentral* Within three (3) days from approval by the SEC of its bond issue, a QB shall notify the appropriate department of the BSP of the approval, attaching documents required by the SEC for the issuance and registration of the bond issue.

§ 4239Q.4 ***(2008 - 4217Q.5) Minimum features.*** Bond issues by QBs shall have the following minimum features:

a. *Form; issue price; denomination*. The trust indenture and the name of the indenture trustee shall be indicated on the face of the bond certificate.

The SEC-assigned bond registration number and expiry date, if any, shall likewise be indicated, stamped on the face of each bond certificate issued.

Bonds may be issued at face value, at a discount, or at a premium. Minimum denomination shall be ₱20,000.

b. *Term*. The minimum maturity of the bonds shall be four (4) years. No optional redemption before the fourth year shall be allowed.

c. *Interest; manner; form of payment* The bonds shall not be subject to interest rate ceilings prescribed by the Monetary Board or Act No. 2655, as amended.

Interest paid in advance shall not exceed the interest for one (1) year: *Provided,* That interest shall not be paid in kind.

d. *Trust indenture; collaterals; sinking fund*. A trust indenture shall be executed between the issuer and a qualified trust corporation as trustee, which shall neither be an affiliate nor a subsidiary of the issuer.

The following shall be deemed as eligible collateral and shall be maintained at respective values indicated in relation to the face value of the bond issue:

(1)	Government securities	- Aggregate current market value of 100%
(2)	High-grade private securities listed in the big board of stock exchanges	- Aggregate current market value of 150%
(3)	Real estate	- Net book value of 100%
(4)	Unmatured receivables acquired with recourse; lease contracts receivable	- Net book value of 150%
(5)	Unmatured receivables acquired without recourse	- Net book value of 200%

Government and private securities, certificates of title and documents evidencing receivables offered as security shall be physically delivered to the indenture trustee.

Substitution of collaterals shall be allowed: *Provided,* That in no case shall the collateral fall below the herein-required ratios.

The issuer may, at his option, provide for the retirement at maturity of the bond issue through a sinking fund to be deposited with and managed by the indenture trustee.

e. *Bond registry*. The bonds shall be fully registered as to principal and interest. The issuer, its trustee, agent or underwriter must maintain a bond registry duly approved by the SEC for recording, in initial and subsequent transfers, the names of transferees, date of transfer, purchase price and serial numbers of bonds transferred.

§ 4239Q.5 ***(2008 - 4217Q.2) Underwriting of bonds.*** Bond issues may be underwritten by entities including those which are affiliates or subsidiaries of the issuer. The investment of affiliates or subsidiaries in said bond issue shall be subject to:(a) individual and aggregate ceilings of ten percent (10%) and thirty percent (30%), respectively, of the bond issue; and (b) the condition that the investing affiliate or subsidiary does not have any outstanding loan from the issuer or that it shall not incur any indebtedness from the issuer during the period that the investment remains outstanding.

§ 4239Q.6 ***(2008 - 4217Q.6) Reserve requirement.*** A five percent (5%) reserve shall be maintained against all bond issues of QBs.

The form/composition of reserves for bond issues shall be in accordance with the applicable rules on reserve against deposit substitute liabilities and borrowings.

§ 4239Q.7 *(2008 - 4217Q.7) Inapplicability of certain regulations.* Secs. 4235Q and 4236Q shall not apply to bonds issued under these guidelines.

F. (RESERVED)

Sec. 4240Q (Reserved)

G. INTEREST

Sec. 4241Q *(2008 - 4236Q)* Yield/Interest Rates

a. Deposit substitutes of QBs shall not be subject to yield or interest rate ceilings.

b. A matured and an unclaimed deposit substitute shall be payable on demand and shall earn interest or yield from maturity to actual withdrawal or renewal at a rate applicable to a deposit substitute with a maturity of fifteen (15) days.

Secs. 4242Q - 4252Q (Reserved)

H. RESERVES

Sec. 4253Q *(2008 - 4246Q)* Reserves Against Deposit Substitutes. QBs shall maintain regular reserves of eight percent (8%)[1] of deposit substitute liabilities as defined in Section 95 of R.A. No. 7653, regardless of maturities except: (a) borrowings from the BSP through the sale of government securities under repo agreements made in connection with the provisions of Sec. 4601Q; (b) deposit substitutes arising from special financing programs of the Government and/or international FIs; (c) interbank call loan transactions under Sec. 4343Q; and (d) bonds under Sec. 4239Q for which the reserve requirement shall be five percent (5%).

On top of the regular reserve requirements, an additional eleven percent (11%)[2] liquidity reserves against deposit substitute liabilities (except Items *"a"* to *"d"* above) of QBs shall be imposed which may be maintained in the form prescribed in Item *"a"* of Sec.. 4254Q. Any deficiency shall be in the form prescribed in Item *"b"* of Sec. 4254Q.

Provided, That deposit substitutes evidenced by repo agreements covering government securities up to the amount equivalent to the adjusted Tier 1 capital of the QB shall be subject to the statutory reserve of two percent (2%)[3]: *Provided, further,* That such rate shall apply only to repo agreements, the documentation of which conforms with, and were delivered to a BSP accredited third party custodian as required under existing BSP regulations.

(As amended by Circular No. 632 dated 19 November 2008)

Sec. 4254Q *(2008 - 4246Q.1) Composition of reserves.* The composition of the reserves shall be as follows:

a. Not more than the percentage of liquidity reserves required under Sec. 4253Q shall be maintained in the Reserve Deposit Account (RDA) with the BSP or may be in the form of the following: *Provided,* That it complies with the guidelines shown in *Appendix Q-41*.

(1) Short-term market-yielding government securities purchased directly from the BSP-Treasury Department;

(2) NDC Agri-Agra ERAP Bonds, regardless of maturity; and

(3) Poverty Eradication and Alleviation Certificates (PEACe) bonds only to the extent of the original gross issue proceeds determined at the time of the auction, plus

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[1] Under Circular No. 632 dated 19 November 2008, the reduction in regular reserves shall be effective the reserve week starting 14 November 2008.

[2] From 10% to 11% under Circular No. 491 dated 21 July 2005, effective the reserve week starting 15 July 2005.

[3] The statutory reserve of two percent (2%) may not be availed of pending:
(1) the issuance of the pertinent market convention acceptable to BSP that shall govern deposit substitutes transactions evidenced by repo agreements covering government securities; and
(2) the opening for the purpose of a separate RoSS account with the Bureau of the Treasury by the BSP-accredited third party custodian.

capitalized interest on the underlying zero-coupon Treasury Notes as and when the corresponding interest is earned over the life of the bonds.

Any deficiency in the liquidity reserve shall continue to be in the forms or modes prescribed under existing regulations for the composition of required reserves.

b. The balance shall be as follows:

(1) At least ten percent (10%) in the form of deposit balances with the BSP;

(2) A maximum of seventy-five percent (75%) in the form of government securities; and

(3) The balance in the form of demand deposit accounts with banks which are not restricted as to withdrawal or use for current operations but not with FIs which have been closed and are under receivership or liquidation.

For purposes of this Subsection, government securities eligible as reserves against deposit substitute liabilities of QBs as referred to in Item *"b(2)"* above shall be limited to bonds or other evidences of indebtedness representing direct obligations of the government of the Republic of the Philippines having the following minimum features/conditions:

(i) The securities must bear an interest rate of not more than four percent (4%) per annum, must be non-negotiable and shall carry BSP support; and

(ii) The instrument must expressly state in its face the amount, maturity date and interest rate of the obligation.

A list of reserves-eligible and non-eligible securities may be found in *Appendix Q-9*.

Other government securities being used for reserve purposes shall continue to be eligible as such: *Provided,* That whenever said securities shall have matured, they shall be replaced by securities carrying the above features.

Securities held as reserves shall be valued at cost of acquisition, and the QB may freely alter its composition: *Provided,* That any substitution or acquisition satisfies the eligibility requirements prescribed above: *Provided, further,* That the QB notifies the BSP of any such change not later than the reporting day following the change.

Securities counted as reserves which are hypothecated or encumbered in any way or earmarked for any other purpose shall automatically lose their eligibility as reserves.

Only the buying/lending QB in a resale agreement covering eligible government securities may use such securities as reserves against deposit substitute liabilities. Conversely, the selling/borrowing QB in a repo agreement covering eligible government securities may not use such securities as reserves against deposit substitute liabilities.

The reserve eligibility of government securities under the reverse repo operations of the BSP shall be suspended during the term of the repo agreement. The phrase *non-reserve eligible* shall be stamped on the face of the custodian receipt being issued by the BSP to buyer FIs.

(As amended by Circular Nos. 551 dated 17 November 2006 and 539 dated 09 August 2006)

§ 4254Q.1 ***(2008 - 4246Q.5) Matured and unclaimed deposit substitutes.*** Matured and unclaimed deposit substitutes shall continue to be subject to reserves.

§ 4254Q.2 (*Reserved*)

§ 4254Q.3 ***(2008 - 4246Q.7) Interest on reserve deposit with Bangko Sentral*** Deposits maintained by QBs with the BSP up to forty percent (40%) of their reserve requirement (excluding the percentage of liquidity reserves required on deposit substitute liabilities of QBs under Sec. 4253Q) shall be paid interest at four percent (4%) per annum based on the average daily balance of said deposits to be credited quarterly.

The computation of quarterly interest payments credited to the QBs' DDAs with BSP are shown in *Appendix Q-27*.

Effective 1 July 2003, published interest rates that will be applied on BSP's Regular DDAs of QBs shall be inclusive of the ten percent (10%) Value Added Tax (VAT).

§ 4254Q.4 ***(2008 - 4246Q.6) Book entry method for reserve securities.*** Transactions concerning reserve-eligible securities shall be entered in the respective securities account of each QB with the BSP and shall be evidenced by securities account debit or credit advices to be promptly furnished the institution/s concerned. No certificates shall be issued for any purpose. Transactions with third parties other than the BSP shall not be recognized.

Sec. 4255Q ***(2008 - 4246Q.4)*** **Exemptions** Certificates of assignment issued with recourse by QBs under the IGLF Program are not covered by the reserve requirements.

Sec. 4256Q ***(2008 - 4246Q.2)*** **Computation of reserve position.** The reserve position of any QB and the penalty on reserve deficiency shall be computed based on a seven (7)-day week, starting Friday and ending Thursday, including Saturdays, Sundays, public special/legal holidays, non-business days, unexpected declared non-business days or declared half-day holidays and days when there is no clearing: *Provided*, That with reference to public special/legal holidays, non-business unexpected declared non-business days, declared halfday holidays and days when there is no clearing, the reserve position as calculated at the close of the business day immediately preceding such public special/legal holidays, non-business days and unexpected declared non-business day/s and declared half-day holidays and days when there is no clearing, shall apply thereon. For this purpose, the principal office in the Philippines and all other offices located therein shall be treated as a single unit.

The guidelines on the computation of a bank's reserve position during public sector holidays are shown in *Appendix Q-49* .

The required reserves in the current period (reference reserve week) shall be computed based on the corresponding levels of deposit substitute liabilities of the prior week.

(As amended by M-2008-025 dated 13 August 2008)

§§4256Q.1 - 4256Q.4 ***(Reserved)***

§ 4256Q.5 ***(2008 - 4246Q.8) Guidelines in calculating and reporting to the BSP the required reserves on deposit substitutes evidenced by repurchase agreements covering government securities***

a. The Supervisory Data Center (SDC) shall determine the maximum allowable amount of repo agreements covering government securities that will qualify for the reduced statutory reserve requirements of two percent (2%). It shall be based on the amount reported by QBs in their weekly Consolidated Daily Report of Condition. The adjusted Tier 1 capital reported daily should approximate the quarterly adjusted Tier 1 capital as submitted by banks in compliance with the provisions of Sec. 4115Q.

b. Any material differences that may be noted by the SDC between the daily and the quarterly report shall be considered as erroneous reporting and shall be subject to the penalties under existing regulations. The SDC shall also make a re-run of its computation of the QB's reserve position and in the event that the reserve position resulted to a reserve deficiency/ies, the corresponding penalties on reserve deficiencies shall also apply.

c. The lagged system in the measurement of a QB's reserve requirement, as provided in Sec.4256Q, shall also be

adopted in the calculation of the two percent (2%) statutory reserve requirements for repo agreements covering government securities.

d. Deposit substitutes evidenced by repo agreements covering government securities in excess of the adjusted Tier 1 capital shall be treated as regular deposit substitutes and shall be subject to the regular statutory and liquidity reserve requirements under existing regulations.

Sec.4257Q *(2008 - 4246Q.3)* Reserve Deficiencies; Sanctions

a. Whenever the reserve position of any QB computed in the manner specified in Sec.4256Q is below the required minimum, the QB concerned shall pay the BSP one-tenth of one percent (1/10 of 1%) per day on the amount of the deficiency or the prevailing ninety-one (91)- day T-Bill rate plus three (3) percentage points, whichever is higher: *Provided, however,* That the QB shall be permitted to offset any reserve deficiency occurring one (1) or more days of the week covered by the report against excess reserves which it may hold on other days of the same week, and shall be required to pay the penalty only on the average daily net deficiency during the week.

In case of abuse, the QB shall automatically lose the privilege of offsetting reserve deficiency in the aforesaid manner until such time that it maintains its daily reserve position at the required minimum for at least two (2) consecutive weeks.

As used in this Section, *abuse* in the privilege of offsetting reserve deficiencies against excess reserves shall mean having reserve deficiencies occurring four (4) or more times during any given week for two (2) consecutive weeks, whether or not resulting in net weekly deficiencies.

b. In cases where the QB has chronic reserve deficiency on deposit substitute liabilities, the Monetary Board may (1) limit or prohibit the making of new loans or investments by the QB concerned; (2) prohibit the declaration of cash dividends; and/or (3) impose such other sanctions, as it may deem necessary. The board of directors of such QB shall be notified of such chronic reserve deficiency and the penalties therefor, and shall be required to immediately correct the reserve position of the QB.

As used in this Section, the following terms shall have the following meanings:

Chronic reserve deficiency shall mean having net reserve deficiency for two (2) consecutive weeks.

New loan and new investment shall refer to any loan and any investment involving disbursement of funds.

c. Fines on legal reserve deficiencies on deposit substitute liabilities shall be paid by the QB in accordance with Sec. 4902Q: *Provided,* That where the credit balance of the QB's demand deposit account (DDA) with the BSP is insufficient and it fails to settle the assessment within fifteen (15) days from receipt, the Monetary Board may limit or prohibit the making of new loans or investments by the QB.

I. (RESERVED)

Secs. 4258Q - 4269Q (Reserved)

J. BORROWINGS FROM THE BANGKO SENTRAL

Sec. 4270Q *(2008 - 4276Q)* Repurchase Agreements with the Bangko Sentral. Repo agreements with the BSP under its open market operations (OMOs) shall be governed by the provisions of Subsec. 4601Q.1.

Secs. 4271Q - 4277Q (Reserved)

Sec. 4278Q Enhanced Intraday Liquidity Facility. The ILF is a smoothening mechanism which is available to eligible participant QBs in the Philippine Payments and Settlements System (PhilPaSS) to support their liquidity requirements and avoid payment gridlocks in PhilPaSS. The revised features of the enhanced intraday liquidity facility are shown in *Appendix Q-13-B*.
(As superseded by the MOA between the BSP, BTr, BAP and Money Market Association of the Philippines dated 25 March 2008)

Secs. 4279Q - 4280Q (Reserved)

K. OTHER BORROWINGS

Sec. 4281Q Borrowings from the Government. QBs shall not borrow any fund or money from the Government and government entities, through the issuance or sale of its acceptances, notes or other evidence of debt, except as may be authorized by existing statutes.

§ 4281Q.1 ***Definition of terms.*** For purposes of this Section, the following terms shall have the meaning indicated unless the context clearly indicates otherwise:

a. *Fund or money from the Government and government entities* includes public moneys of every sort, whether pertaining to the National Government, province, city, municipality, or other branch or agency of the Government, including government-owned or controlled corporations (GOCCs) as defined herein, and shall comprise *"revenue funds", "trust funds"*, and *"depository funds"* as these terms are defined in the Revised Administrative Code of 1987, and deposits of, borrowings from, and all other liabilities to, the Government and government entities.

b. *GOCCs* shall refer to GOCCs which are created by special laws. It shall exclude government FIs such as the Development Bank of the Philippines (DBP), Land Bank of the Philippines (LBP) and Al-Amanah Islamic Investment Bank of the Philippines, corporations which are organized as subsidiaries of GOCCs under the provisions of the Corporation Law (Act No. 1459, as amended) or the Corporation Code (BP Blg. 68) and private corporations which are taken over by GOCCs.

Secs. 4282Q - 4298Q (Reserved)

L. GENERAL PROVISION ON SANCTIONS

Sec. 4299Q General Provision on Sanctions. Any violation of the provisions of this Part shall be subject to Sections 36 and 37 of R.A. No. 7653.

The guidelines for the imposition of monetary penalty for violations/offenses with sanctions falling under Section 37 of R.A. No. 7653 on QBs, their directors and/or officers are shown in *Appendix Q-39*.

PART THREE

LOANS, INVESTMENTS AND SPECIAL CREDITS

Section 4301Q Management of Risk Assets/Minimum Guidelines on Lending Operations. It shall be the responsibility of the board of directors of a QB to formulate written policies on the extension of credit and risk diversification and to set the guidelines for evaluation of risk assets. Well-defined lending policies and sound lending practices are essential if a QB is to perform its credit-extension function effectively and minimize the risk inherent in any extension of credit. The responsibility should be approached in a way that will provide assurance to the public, the stockholders and supervisory authorities that timely and adequate action will be taken to maintain the quality of the loan portfolio and other risk assets.

a. *Requirement of lending policies* QBs shall have well-defined lending policies which shall ensure that lending shall be upon terms which are in the best interest of the institution and in accordance with existing policy, rules and regulations of the Monetary Board. Such policies shall be in writing to form part of the institution's permanent records and shall be made available for inspection by the Bangko Sentral.

b. *Lending operations, definition* Lending operations refer to any credit accommodation and purchase of receivables and commercial papers, including purchase of commercial papers in the secondary market.

c. *Creditworthiness of borrowers* Before extending credit in any form, the QB must exercise proper caution to ascertain that the debtors, co-makers, endorsers, sureties and/or guarantors are capable of fulfilling their commitments. For this purpose, credit investigations must be conducted and appropriate statements of assets and liabilities and of income and expenditures shall be required of credit applicants.

d. *Amounts, purpose and terms of credit accommodations*. Loans/credit accommodations shall be granted only in amounts and for periods necessary for the completion of the operations to be financed, and for purposes which are attuned to government economic policies. The amount and period of the loan shall be justified by the financial statements submitted or by specific feasibility/project studies for a particular operation to be financed by the loan applied for.

e. *Documentation of loans*. All loans/credit extensions shall be supported by evidences of indebtedness and/or loan agreements which shall contain, among other things, a statement of the purpose of the loan and a program of repayment of the obligation.

f. *Credit files*. Adequate credit files of borrowers shall be maintained which shall contain documents such as credit investigation reports, balance sheets, statements of assets and liabilities, income and expense statements, income tax returns, bank and trade checkings, and other documents/papers showing information which form the bases for the credit extension.

g. *Periodic review*. A periodic review of the loan portfolio and the credit standing of borrowers shall be made.

h. *Arm's length transactions*. A QB shall not relend to or purchase receivables or other obligations of other corporations, majority of the voting stock

of which is owned by subject corporation, unless the terms of the transactions are not more favorable than those of other similar transactions.

§§ 4301Q.1 - 4301Q.5 ***(Reserved)***

§ 4301Q.6 ***Large exposures and credit risk concentrations.*** The following guidelines shall govern managing large exposures and credit risk concentrations in line with the objective of strengthening risk management in the quasi-banking system.

a. *General principles*

(1) A QB can be exposed to various forms of credit risk concentration which if not properly managed may cause significant losses that could threaten its financial strength and undermine public confidence in the QB.

(2) Credit risk concentrations may arise from excessive exposures to individual counterparties, groups of related counterparties and groups of counterparties with similar characteristics (e.g., counterparties in specific geographical locations, economic or industry sectors).

(3) Diversification of risk is essential in quasi-banking. Many past QB failures have been due to credit risk concentrations of some kind. It is essential for QBs to prevent undue credit risk concentrations from excessive exposures to particular counterparties, industries, economic sectors, regions or countries.

(4) While concentration of credit risks is inherent in quasi-banking and cannot be totally eliminated, they can be limited and reduced by adopting proper risk control and diversification strategies. Safeguarding against credit risk concentrations should form an important component of a QB's risk management system.

(5) The board of directors of a QB shall be responsible for establishing and monitoring compliance with policies governing large exposures and credit risk concentrations of the QB. The board should review these policies regularly (at least annually) to ensure that they remain adequate and appropriate for the QB. Subsequent changes to the established policies must be approved by the board.

(6) The policy on large exposures and credit risk concentrations shall, at a minimum, covers the following:

(a) Exposure limits that are reasonable in relation to capital and resources for –

(i) Various types of borrowers/ counterparties (e.g. government, banks and other FIs, corporate and individual borrowers);

(ii) A group of related borrowers/ counterparties;

(iii) Individual industry sectors;

(iv) Individual countries; and

(v) Various types of investments.

(b) The circumstances in which the above limits can be exceeded and the party authorized to approve such excesses, e.g., the QB's board of directors or credit committee with delegated authority from the board;

(c) The delegation of credit authority within the QB for approving large exposures;

(d) The procedures for identifying, reviewing, managing and reporting large exposures of the QB;

(e) The definition of exposure. QBs should take into account the nature of their business and the complexity of their products. In any case, a QB's exposures to a counterparty should include its on and off-balance sheet exposures and indirect exposures; and

(f) The criteria to be used for identifying a group of related persons;

(7) The board and senior management of a QB should ensure that:

(a) Adequate systems and controls are in place to identify, measure, monitor and report large exposures and credit risk

concentrations of the QB in a timely manner; and

(b) Large exposures of the QB are kept under regular review. *"Large exposures"* shall refer to exposures to a counterparty or a group of related counterparties equal or greater than five percent (5%) of QB's qualifying capital as defined under Section 4115Q.

(8) A QB should, where appropriate, conduct stress testing and scenario analysis of its large exposures to assess the impact of changes in market conditions or key risk factors (e.g. economic cycles, interest rate, liquidity conditions or other market movements) on its profile and earnings.

(9) It is expected that QBs would generally observe a lower internal SBL than the prescribed limit of twenty-five percent (25%) as a matter of sound practice.

b. *Monitoring of large exposures/credit risk concentrations*

(1) QBs should have a central liability record (preferably based on automated system) for each loan exposure. QBs should be able to monitor such exposures against prescribed and internal limits on a daily basis.

(2) Every QB should have adequate management information and reporting systems that enable management to identify credit risk concentrations within the asset portfolio of the QB or of the group (including subsidiaries and overseas branches) on a timely basis. If a concentration does exist, QBs should reduce it in accordance with their prescribed policies. Large exposures shall be subject to more intensive monitoring.

(3) QBs should ensure that their internal or external auditors conduct at least an annual review of the quality of large exposures and controls to safeguard against credit risk concentrations. Their review should ascertain whether:

(a) The QB's relevant policies, limits and procedures are complied with; and

(b) The existing policies and controls remain adequate and appropriate for the QB's business.

(4) Management should take prompt corrective action to address concerns and exceptions raised.

(5) There should also be an independent compliance function to ensure that all relevant internal and prescribed requirements and limits are complied with. Breaches of prescribed requirements and deviations from established policies and limits should be reported to senior management in a timely manner.

c. *Unsafe and unsound practice*

Non-observance of the principles and the requirements of Items *"a"* and *"b"* above may be a ground for a finding of unsafe and unsound practice under Section 56 of R.A. No. 8791 *(Appendix Q-24)* and may be subject to appropriate sanction as may be determined by the Monetary Board

d. *Notification requirements*

A QB must inform BSP immediately where it has concerns that its large exposures or credit risk concentrations have the potential to impact materially upon its capital adequacy, along with proposed measures to address these concerns.

e. *Reporting*

QB's records on monitoring of large exposures shall be made available to the BSP examiners for verification at any given time. When warranted, the BSP may impose additional reporting requirements on QB in relation to its large exposures and credit risk concentrations.

f. *Sanction*

Any failure or delay in complying with the requirements under Items *"d"* and *"e"* of this Subsection shall be subject to penalty applicable to those involving major reports.
(As amended by Circular No. 640 dated 16 January 2009)

Sec. 4302Q Loan Portfolio and Other Risk Assets Review System. To ensure that timely and adequate management action is taken to maintain the quality of the loan portfolio and other risk assets and that adequate loss reserves are set up and maintained at a level sufficient to absorb the loss inherent in the loan portfolio and other risk assets, QBs shall establish a system of identifying and monitoring existing or potential problem loans and other risk assets and of evaluating credit policies vis-a-vis prevailing circumstances and emerging portfolio trends. Management must also recognize that loss reserve is a stabilizing factor and that failure to account appropriately for losses or make adequate provisions for estimated future losses may result in misrepresentation of the QB's financial condition.

The system of identifying and monitoring problem loans and other risk assets and setting up of allowance for probable losses shall include, but is not limited to, the guidelines in *Appendix Q-10*.

(As amended by Circular Nos. 622 dated 16 September 2008 and 520 dated 20 March 2006)

§ 4302Q.1 *Provisions for losses; booking.* The board of directors of QBs are responsible for ensuring that their institutions have controls in place to determine the allowance for probable losses on loans, other credit accommodations, advances and other assets consistent with the institutions' stated policies and procedures, generally accepted accounting principles (GAAP), the BSP rules and regulations and the safe and sound banking practices. The board of directors, in fulfilling this responsibility, shall require management to develop and maintain an appropriate, systematic and uniformly applied process consistent and in compliance with existing BSP rules and regulations to determine the amount of reserves for bad debts or doubtful accounts or other contingencies.

The specific allowance for probable losses for classified loans and other risk assets and the general loan loss provision as required in *Appendix Q-10* shall be set up immediately.

§ 4302Q.2 *Sanctions.* Non-compliance with the requirement to book the valuation reserves required under the preceding Subsection shall be a ground for the imposition of any or all of the following sanctions:

a. Denial of requests for authority to establish branches/offices; and

b. Fine of P5,000 a day, counted as follows:

(1) from the date the QB was informed that the recommendation of the appropriate department of the SES was confirmed by the Monetary Board up to the date that said recommended valuation reserves were actually booked, in case of the allowance for probable losses for loans and other risk assets classified as *Substandard (Unsecured), Doubtful* and *Loss* as required by the BSP; and

(2) from the dates prescribed under the preceding Subsection up to the date of the actual booking in cases of the two percent (2%) general provision for probable loan losses, the twenty-five percent (25%) allowance for probable losses on secured loans classified as *Substandard*, and the five percent (5%) allowance for probable losses on *Loans Especially Mentioned*.

A. LOANS IN GENERAL

Sec. 4303Q *(2008 - 4306Q)* Loan Limit to a Single Borrower. The total liabilities of any person, company, corporation or firm, to a QB for money borrowed, excluding (a) loans secured by obligations of the BSP or of the Philippine Government; (b) loans fully guaranteed by the government as to

the payment of principal and interest; (c) loans fully secured by US Treasury Notes and other securities issued by central governments and central banks of foreign countries with the highest credit quality given by any two (2) internationally accepted rating agencies; (d) loans to the extent covered by the hold-out on or assignment of, deposits maintained in the lending QB and held in the Philippines; (e) loans and acceptances under letters of credit to the extent covered by margin deposits; and (f) other loans or credits which the Monetary Board may, from time to time, specify as non-risk assets, shall at no time exceed twenty-five percent (25%) of the combined capital accounts as defined in Sec. 4111Q.

The total liabilities of any borrower may amount to a further fifteen percent (15%) of the combined capital accounts of such QB: *Provided,* That the additional liabilities are adequately secured by real estate mortgage, assignment or pledge of readily marketable bonds and other high-grade debt securities, except those issued by the lending entity.

The total amount of loans, credit accommodations and guarantees prescribed in the first paragraph may be increased by an additional twenty-five percent (25%) of the net worth of such QB: *Provided,* That the additional loans, credit accommodations and guarantees are for the purpose of undertaking infrastructure and/or development projects under the Public-Private Partnership (PPP) Program of the government duly certified by the Secretary of Socio-Economic Planning; *Provided, further*, That the total exposures of the QB to any borrower pertaining to such infrastructure and/or development projects under the PPP Program shall not exceed twenty-five percent (25%) of the net worth of such QB: *Provided, furthermore,* That the additional twenty-five percent (25%) shall only be allowed for a period of three (3) years from 28 December 2010: *Provided, finally,* That the credit risk concentration arising from total exposures to all borrowers pertaining to such infrastructure and/or development projects under the PPP Program shall be considered by the QB in its internal assessment of capital adequacy relative to its overall risk profile and operating environment. Said loans, credit accommodations and guarantees based on the contracted amount as of the end of the three (3)-year period shall not be increased but may be reduced and once reduced, said exposures shall not be increased thereafter.

For purposes of this Section, the term *liabilities* shall mean the direct liability of the maker or acceptor of paper discounted with or sold to such QB and the liability of the endorser, drawer or guarantor who obtains a loan from or discounts paper with or sells papers under his guaranty to such QB and shall include in the case of liabilities of a co-partnership or association, the liabilities of the several members thereof and shall include, in the case of liabilities of a corporation, all liabilities of its subsidiaries: *Provided,* That even in cases where the parent corporation, co-partnership or association has no liability to the QB, the liabilities of subsidiary corporations or members of the co-partnership or association shall be combined for purposes of the single borrower's limit (SBL).

(As amended by Circular No. 700 dated 06 December 2010)

§ 4303Q.1 ***(2008 - 4306Q.1) Exclusions from loan limit.*** In addition to those enumerated in Sec. 4303Q, the total liabilities of a commercial paper issuer for commercial papers held by a QB as a firm underwriter shall not be counted in determining compliance with the SBL within a period of 180 days from the acquisition of the commercial paper by a

QB: *Provided*, That in no case shall such liabilities exceed five percent (5%) of the net worth of the selling agent beyond the normal applicable SBL.

§ 4303Q.2 ***(2008 - 4306Q.2) Contingent liabilities included in loan limit*** Outstanding foreign and domestic standby and deferred letters of credit less margin deposits, and outstanding guarantees, the nature of which requires the guarantor to assume the liabilities/obligations of third parties in case of their inability to pay, shall be included in determining the SBL except those fully secured by cash, hold-out on deposit substitutes, or government securities.

§§ 4303Q.3 - 4303Q.4 ***(Reserved)***

§ 4303Q.5 ***(2008 - 4306Q.3) Sanctions*** Violations of the provisions of the foregoing rules shall be subject to the following sanctions/penalties:

a. *Fines*. Fines of one-tenth of one percent (1/10 of 1%) of the excess but not to exceed P30,000 a day for each violation, reckoned from the date the excess started up to the date when such excess was eliminated, shall be assessed on the QB.

b. *Other sanctions*

First Offense

Reprimand for the directors/officers who approved the credit line or availment which resulted in the excess with a warning that subsequent violations will be subject to more severe sanctions.

Subsequent offenses

(1) For the duration of each violation, imposition of a fine of P500 a day for each of the directors/officers who approved the credit line or availment which resulted in an excess.

(2) Suspension of the QB from branching privileges until the excess is eliminated.

Sec. 4304Q ***(2008 - 4312Q)*** **Grant of Loans and Other Credit Accommodations.** The following regulations shall be observed in the grant of loans and other credit accommodations.

§ 4304Q.1 ***(2008 - 4312Q.1) General guidelines.*** Consistent with safe and sound business practices, a QB shall grant loans or other credit accommodations only in amounts and for the periods of time essential for the effective completion of the operation to be financed.

Before granting loans or other credit accommodations, a QB must ascertain that the borrower, co-maker, endorser, surety and/or guarantor, if applicable, is/are financially capable of fulfilling his/their commitments to the QB. For this purpose, a QB shall obtain adequate information on his/their credit standing and financial capacities.

In addition to the usual information sheet about the borrower, a QB shall require from the credit applicant the following:

a. A copy of the latest Income Tax Return (ITR) of the borrower and his co-maker, if applicable, duly stamped as received by the BIR;

b. Except as otherwise provided by law and in other regulations, if the borrower is engaged in business, a copy of the borrower's latest financial statements as submitted for taxation purposes to the BIR; and

c. A waiver of confidentiality of client information and/or an authority of the QB to conduct random verification with the BIR in order to establish authenticity of the ITR and accompanying financial statements submitted by the client.

The documents under Items *"a"* and *"b"* above shall be required to be submitted annually for as long as the loan and/or credit accommodation is outstanding.

The consistency of the data/figures in said ITRs and financial statements shall also be checked and considered in the evaluation of the financial capacity and creditworthiness of credit applicants. The waiver of confidentiality of client information and/or an authority of the QB to conduct random verification with the BIR need not be submitted annually since once submitted these documents remain valid unless revoked.

Should the document(s) submitted prove to be spurious or incorrect in material detail, the QB may terminate any loan or other credit accommodation granted on the basis of said document(s) and shall have the right to demand immediate repayment or liquidation of the obligation. Moreover, the QB may seek redress from the court for any harm done by the borrower's submission of spurious documents.

The required submission of additional documents shall cover loans, other credit accommodations, and credit lines granted, restructured, renewed or extended after 02 November 2006 including any availment and/or re-availment against existing credit lines, except:

(1) Microfinance loans as defined under Subsec. X361.1 (a);

(2) Loans to registered BMBEs;

(3) Interbank loans;

(4) Loans secured by hold-outs on or assignment of deposits or other assets considered non-risk by the Monetary Board;

(5) Loans to individuals who are not required to file ITRs under BIR regulations, as follows:

(a) Individuals whose gross compensation income does not exceed their total personal and additional exemptions, or whose compensation income derived from one (1) employer does not exceed P60,000 and the income tax on which has been correctly withheld;

(b) Those whose income has been subjected to final withholding tax;

(c) Senior citizens not required to file a return pursuant to R.A. No. 7432, as amended by R.A. No. 9257, in relation to the provisions of the National Internal Revenue Code (NIRC) or the Tax Reform Act of 1997; and

(d) An individual who is exempt from income tax pursuant to the provisions of the NIRC and other laws, general or special; and

(6) Loans to borrowers, whose only source of income is compensation and the corresponding taxes on which has been withheld at source: *Provided*, That the borrowers submitted, in lieu of the ITR, a copy of their Employer's Certificate of Compensation Payment/Tax Withheld (BIR Form 2316) or their payslips for at least three (3) months immediately preceding the date of loan application.

Loans to micro and small enterprises which are not specifically exempted from the additional documentary requirements specified under the third paragraph of this Subsection shall be exempted from said additional documentary requirement up to 31 December 2011.

Consumer loans, with original amounts not exceeding P2.0 million, are exempted from updating requirements or the required annual submission of the same requirements forwarded during the initial submission under this Subsection but not in their restructuring, renewal, or extensions or availment/re-availment against existing credit lines: *Provided*, That these loans are supported by ITRs or by BIR Form 2316 or payslips for at least three (3) months immediately preceding the date of loan application, and financial statements submitted for taxation purposes to the BIR, as may be applicable, at the time the loans were granted, restructured, renewed, or

extended.

For purposes of this Subsection, the following definitions shall apply:

1. *Micro and small enterprises* shall be defined as any business activity or enterprise engaged in industry, agribusiness and/or services whether single proprietorship, cooperative, partnership or corporation whose total assets, inclusive of those arising from loans but exclusive of the land on which the particular business entity's office, plant and equipment are situated, must have a value of up to P3.0 million and P15.0 million respectively, or as may be defined by the SMED Council or other competent government agency.

2. *Consumer loans* is defined to include housing loans, loans for purchase of car, household appliance(s), furniture and fixtures, loans for payment of educational and hospital bills, salary loans and loans for personal consumption, including credit card loans.

(As amended by Circular Nos. 694 dated 14 October 2010, 622 dated 16 September 2008, 607 dated 30 April 2008 and 549 dated 09 October 2006)

§ 4304Q.2 ***(2008 - 4312Q.2) Purpose of loans and other credit accommodations*** Before granting a loan or other credit accommodation, QBs shall ascertain the purpose of the loan or other credit accommodation which shall be clearly stated in the application and in the contract between the QB and borrower. The proceeds of a loan or other credit accommodation shall be utilized only for the purpose(s) stated in the application and contract; otherwise, the QB may terminate the loan or other credit accommodation and demand immediate repayment of the obligation. Notwithstanding the preceding sentence, the proceeds of a loan or other credit accommodation may be utilized by the borrower for a purpose(s) other than that originally stated in the application and contract: *Provided,* That such other purpose(s) is/are among those for which the lending QB may grant loans and other credit accommodations under existing laws and regulations: *Provided, further,* That such utilization shall be with prior written approval of duly authorized officer(s)/ committee/board of directors of the lending QB and such written approval shall form part of the contract between the QB and the borrower.

(Circular No. 622 dated 16 September 2008)

§ 4304Q.3 ***(2008 - 4312Q.3) Prohibited use of loan proceeds.*** QBs are prohibited from requiring their borrowers to acquire shares of stock of the lending QB out of the loan or other credit accommodation proceeds from the same QB.

(Circular No. 622 dated 16 September 2008)

§ 4304Q.4 ***(2008 - 4312Q.4) Signatories.*** QBs shall require that loans and other credit accommodations be made under the signature of the principal borrower and, in the case of unsecured loans and other credit accommodations to an individual borrower, at least one (1) co-maker, except that a co-maker is not required when the principal borrower has the financial capacity and a good track record of paying his obligations.

(As amended by Circular No. 622 dated 16 September 2008)

§§ 4304Q.5 - 4304Q.9 ***(Reserved)***

§ 4304Q.10 ***Minimum required disclosure.*** QBs shall provide a table of the applicable fees, penalties and interest rates on loan transactions, including the period covered by and the manner of and reason for the imposition of such penalties, fees and interests; fees and applicable conversion reference rates for third currency transactions, in plain sight and language,

on materials for marketing loans, such as brochures, flyers, primers and advertising materials, on loan application forms, and on billing statements: *Provided,* That these disclosures are in addition to the full disclosure of the fees, charges and interest rates in the terms and conditions of the loan agreement found elsewhere on the application form and billing statement: *Provided further,* That such table of fees, penalties and interest rates shall be printed in plain language and in bold black letters against a light or white background, and using the minimum Arial 12 theme font and size, or its equivalent in readability, and on the first page, if the applicable document has more than one (1) page.

Transitory provision: QBs shall be given a period of 120 days from 6 January 2011 to fully implement the required disclosure requirements.

(Circular No. 702 dated 15 December 2010)

§ 4304Q.11 *Unfair collection practices* QBs, collection agencies, counsels and other agents may resort to all reasonable and legally permissible means to collect amounts due them under the loan agreement: *Provided,* That in the exercise of their rights and performance of duties, they must observe good faith and reasonable conduct and refrain from engaging in unscrupulous or untoward acts. Without limiting the general application of the foregoing, the following conduct is a violation of this Subsection:

a. the use or threat of violence or other criminal means to harm the physical person, reputation, or property of any person;

b. the use of obscenities, insults, or profane language which amount to a criminal act or offense under applicable laws;

c. disclosure of the names of borrowers who allegedly refuse to pay debts, except as allowed under Subsec. 4304Q.12;

d. threat to take any action that cannot legally be taken;

e. communicating or threat to communicate to any person credit information which is known to be false, including failure to communicate that a debt is being disputed;

f. any false representation or deceptive means to collect or attempt to collect any debt or to obtain information concerning a borrower; and

g. making contact at unreasonable/ inconvenient times or hours which shall be defined as contact before 6:00 A.M. or after 10:00 P.M., unless the account is past due for more than sixty (60) days or the borrower has given express permission or said times are the only reasonable or convenient opportunities for contact.

QBs shall inform their borrowers in writing of the endorsement of the collection of their account to a collection agency/agent, or the endorsement of their account from one collection agency/agent to another, at least seven (7) days prior to the actual endorsement. The notification shall include the full name of the collection agency and its contact details: *Provided*, That the required notification in writing shall be included in the terms and conditions of the loan agreement. QBs shall adopt policies and procedures to ensure that personnel handling the collection of accounts, whether these are in-house collectors, or third-party collection agents, shall disclose his/her full name/true identity to the borrower.

(As amended by Circular No. 702 dated 15 December 2010)

§4304Q.12 *Confidentiality of information.* QBs shall keep strictly confidential the data on the borrower or consumer, except under the following circumstances:

a. disclosure of information is with the consent of the borrower or consumer;

b. release, submission or exchange of customer information with other financial institutions, credit information bureaus, lenders, their subsidiaries and affiliates;

c. upon orders of court of competent jurisdiction or any government office or agency authorized by law, or under such conditions as may be prescribed by the Monetary Board;

d. disclosure to collection agencies, counsels and other agents of the QB to enforce its rights against the borrower;

e. disclosure to third party service providers solely for the purpose of assisting or rendering services to the QB in the administration of its lending business; and

f. disclosure to third parties such as insurance companies, solely for the purpose of insuring the QB from borrower default or other credit loss, and the borrower from fraud or unauthorized charges.

(Circular No. 702 dated 15 December 2010)

§§ 4304Q.13 - 4304Q.14 *(Reserved)*

§ 4304Q.15 *Sanctions.* Violations of the provisions of Subsecs. 4304Q.10 to 4304Q.12 shall be subject to any or all of the following sanctions depending upon their severity:

a. *First offense*. Reprimand for the directors/officers responsible for the violation;

b. *Second offense*. Disqualification of the bank concerned from the credit facilities of the BSP except as may be allowed under Section 84 of R. A. No. 7653;

c. *Subsequent offense/s:*

i. Prohibition on the QB concerned from the extension of additional credit accommodation against personal security; and

ii. Penalties and sanctions provided under Sections 36 and 37 of R. A. No. 7653.

(Circular No. 702 dated 15 December 2010)

Sec. 4305Q *(2008 - 4307Q)* Interest and Other Charges. The following rules shall govern the rates of interest on loans by QBs.

§ 4305Q.1 *(2008 - 4307Q.6) Rate of interest in the absence of stipulation.* The rate of interest for the loan or forbearance of any money, goods or credit and the rate allowed in judgments, in the absence of express contract as to such rate of interest, shall be twelve percent (12%) per annum.

§ 4305Q.2 *(2008 - 4307Q.5) Escalation clause; when allowable.* Parties to an agreement pertaining to a loan or forbearance of money, goods or credits may stipulate that the rate of interest agreed upon may be increased in the event that the applicable maximum rate of interest is increased by law or by the Monetary Board: *Provided,* That such stipulation shall be valid only if there is also a stipulation in the agreement that the rate of interest agreed upon shall be reduced in the event that the applicable maximum rate of interest is reduced by law or by the Monetary Board: *Provided, further,* That the adjustment in the rate of interest agreed upon shall take effect on or after the effectivity of the increase or decrease in the maximum rate of interest.

§ 4305Q.3 *(2008 - 4307Q.2) Floating rates of interest.* The rate of interest on a floating rate loan during each interest period shall be stated based on the Manila Reference Rate (MRR), Treasury Bill Rate (TBR) or other market-based reference rates, plus a margin as may be agreed upon by the parties.

The MRRs for various interest periods shall be determined and announced by the BSP every week and shall be based on the weighted average of the interest rates paid during the immediately preceding week by the ten (10) commercial banks with the highest combined levels of outstanding deposit substitutes and time deposits, in promissory notes issued and time deposits

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received by such banks, of P100,000 and over per transaction account, with maturities corresponding to the interest periods for which such MRRs are being determined. Such rates and the composition of the sample commercial banks shall be reviewed and determined at the beginning of every calendar semester on the basis of the banks' combined levels of outstanding deposit substitutes and time deposits as of May 31 or November 30, as the case may be.

The rate of interest on floating rate loans existing and outstanding as of 23 December 1995 shall continue to be determined on the basis of the MRRs obtained in accordance with the provisions of the rules existing as of 01 January 1989*: Provided, however*, That the parties to such existing floating rate loan agreement are not precluded from amending or modifying their loan agreements by adopting a floating rate of interest determined on the basis of TBR or other market-based reference rates.

Where the loan agreement provides for a floating interest rate, the interest period, which shall be such period of time for which the rate of interest is fixed, shall be such period as may be agreed upon by the parties.

§ 4305Q.4 ***(2008 - 4307Q.7) Accrual of interest earned on loans.*** QBs are allowed to accrue interest earned on loans, subject to the following guidelines and/or procedures.

a. No accrual of interest income is allowed if a loan has become non-performing as defined in Sec. 4309Q. Likewise, interest income shall not be accrued for unmatured loans/receivables with indications that collectibility thereof has become doubtful. These indications include declaration of bankruptcy, insolvency, cessation of operations, or such other conditions of financial difficulties or inability to meet financial obligations as they mature. Separate appropriate records shall be maintained for these non-accruing unmatured loans.

Interest on non-performing loan accounts shall be taken up as income only when actual payments thereon are received.

Interest income on past due loans arising from discount amortization (and not from the contractual interest of the accounts) shall be accrued as provided in PAS 39.

b. Interest earned on an extended or renewed loans may be accrued: *Provided,* That there is no previously accrued but uncollected interest thereon.

Interest income on restructured loans (principal plus capitalized interest thereon) may be accrued: *Provided*, That these are:

(1) In current status; and

(2) Fully secured by real estate with loan value of up to sixty percent (60%) of the appraised value of the real estate security and the insured improvements thereon, and such other first class collaterals as may be deemed appropriate by the Monetary Board.

c. Accrued interest earned but not yet collected/received shall not be considered as profits and/or earnings eligible for dividend declaration and/or profit sharing.

d. A contra account to be designated *Allowance for Uncollected Interest on Loans* shall be set up in accordance with *Appendix 10* if accrued interest receivable on loans or loan installments is still uncollected after three (3) months from the date such loans and loan installments have matured or have become non-performing.

e. The amount representing *Allowance for Uncollected Interest on Loans* may be chargeable against the excess of outstanding valuation reserves for loans and other risk assets as appearing in the QB's books over those recommended by the appropriate department of the SES. The balance thereof, if any, shall be chargeable against operations.

f. For all purposes, the *Allowance for Uncollected Interest on Loans* shall be considered a valuation reserve/allowance against the *Accrued Interest Receivable* account.

§ 4305Q.5 ***(2008 - 4307Q.1) Rate ceilings.*** The rate of interest, including commissions, premiums, fees and other charges on loan transactions, regardless of maturity and whether secured or unsecured, shall not be subject to any ceiling.

§ 4305Q.6 ***(2008 - 4307Q.3) Effect of prepayment.*** If there is no agreement on the rebate of interest in the event of prepayment of the loan, the QB is not under any legal obligation to return the interest corresponding to the period from date of prepayment to the stipulated maturity date of the loan. Any prepayment made by the debtor should not, therefore, affect computation of the effective rate stipulated in the loan contract.

§ 4305Q.7 ***(2008 - 4307Q.4) Loan prepayment.*** The borrower of a QB shall not be prohibited from prepaying a loan. A stipulation requiring the consent of the lending QB to such prepayment shall be contrary to this provision. In case of prepayment in the loan contract, such prepayment shall not be subject to penalty in the absence of any stipulation as to penalty. However, the parties may stipulate that prepayment shall be subject to penalty: *Provided*, That the penalty is not excessive or unconscionable.

Sec. 4306Q ***(2008 - 4308Q)*** **Past Due Accounts.** Past due accounts of a QB shall, as a general rule, refer to all accounts in its loan portfolio, all receivable components of trading account securities and other receivables, as defined in the manual of accounts for NBFIs, which are not paid at maturity.

§ 4306Q.1 ***(2008 - 4308Q.1) Accounts considered past due.*** The following shall be considered as past due:

a. *Loans or receivables payable on demand* - if not paid on the date indicated on the demand letter, or within three (3) months from date of grant, whichever comes earlier;

b. *Bills discounted and time loans, whether or not representing availments against a credit line* - if not paid on the respective maturity dates of the promissory notes;

c. *Customers' liability on drafts under letters of credit/trust receipts:*

(1) Sight Bills - if dishonored upon presentment for payment or not paid within thirty (30) days from date of original entry, whichever comes earlier;

(2) Usance Bills - if dishonored upon presentment for acceptance or not paid on due date, whichever comes earlier; and

(3) Trust Receipts - if not paid on due date.

d. *Bills and other negotiable instruments purchased* - if dishonored upon presentment for acceptance/payment or not paid on maturity date, whichever comes earlier: *Provided, however,* That an out-of-town check and a foreign check shall be considered as past due if outstanding for thirty (30) days and forty-five (45) days, respectively, unless earlier dishonored;

e. *Loans/receivables payable in installments* - the total outstanding balance thereof shall be considered past due in accordance with the following schedule:

Mode of Payment	Minimum Number of Installments in Arrears
Monthly	3
Quarterly	1
Semestral	1
Annual	1

Provided, however, That when the total amount of arrearages reaches twenty percent (20%) of the total outstanding balance of the loan/receivable, the total outstanding balance of the loan/receivable shall be considered as past due, regardless of the number of installments in arrears: *Provided, further,* That for modes of payment other than those

listed above (e.g. daily, weekly or semi-monthly), the entire outstanding balance of the loan/receivable shall be considered as past due when the total amount of arrearages reaches ten percent (10%) of the total loan/receivable balance;

For this purpose, the term *installments* shall refer to principal and/or interest amortizations that are due on several dates as indicated/specified in the loan documents.

f. *Credit card receivables* - if the amount due is not paid within ten (10) days from the deadline indicated in the billing statement; and

g. (*Deleted by Circular No. 202 dated 27 May 1999*)

For the purpose of determining delinquency in the payment of obligations as defined in Subsec. 4143Q.1(e), any due and unpaid loan installment or portion thereof, from the time the obligor defaults, shall be considered as past due.

§ 4306Q.2 ***(2008 - 4308Q.4) Demand loans.*** QBs shall, in case of non-payment of a demand loan, make a written demand within three (3) months following the grant of such loan. The demand shall indicate a period of payment which shall not be later than three (3) months from the date of said demand.

§ 4306Q.3 ***(2008 - 4308Q.2) Renewal/ extension.*** No loan shall be renewed nor its maturity date extended unless the corresponding accrued interest receivable shall have been paid.

§ 4306Q.4 (2008 - 4308Q.3) Restructured loans. A restructured loan shall be immediately classified past due in case of default of any principal or interest payment.

§ 4306Q.5 ***(2008 - 4308Q.5) Write-off of loans as bad debts***

a. QBs, upon approval by their board of directors, may write-off loans, other credit accommodations, advances and other assets against allowance for probable losses (valuation reserves) or current operations as soon as they are satisfied that such loans, other credit accommodations, advances and other assets are worthless as follows:

(1) In the case of secured loans, QBs may write-off loans, other credit accommodations and other assets in an amount corresponding to the booked valuation reserves: *Provided*, That the balance of the secured loans, other credit accommodations, advances and other assets shall remain in the books.

(2) In the cases of unsecured loans, other credit accommodations, advances and other assets, QBs shall write-off said loans, other credit accommodations, advances and other assets in full amount outstanding.

However, write-off of loans, other credit accommodations, advances and other assets considered transactions with DOSRI shall be with prior approval of the Monetary Board.

b. *Definitions*. For purposes of this Section, the following terms are hereby defined as follows:

(1) *Loans*. The term loans shall refer to all the accounts under the loan portfolio of a QB as enumerated in the Manual of Accounts for Quasi-Banks.

(2) *Other credit accommodations*. The term other credit accommodations shall refer to exposures of QBs other than loans such as sales contract receivables, accounts receivables, accrued interest receivables, lease receivables, and rental receivables.

(3) *Advances*. The term advances shall refer to any advance by means of an incidental or temporary overdraft, cash "vale", any advance by means of DAUD and any advances of unearned salary or unearned compensation.

(4) *Other assets*. The term other assets shall refer to investments, placements, ROPAs and all other asset accounts that will not fall under loans and other credit accommodations.

(5) *Bad debts*. The term bad debts shall refer to the definition under Subsec. 4136Q.1.

c. *Reporting requirements*. Notice of write-off of loans, other credit accommodations, advances and other assets shall be submitted in the prescribed form to the appropriate department of the SES at least twenty five (25) banking days prior to the intended date of write-off.

The income tax expense deferred corresponding to the amount of loan, other credit accommodation, advances and other asset written-off considered deductible for income tax purposes shall be recognized and reversed in QB's books.

§ 4306Q.6 ***(Reserved)***

§ 4306Q.7 ***(2008 - 4308Q.6) Updating of information provided to credit information bureaus.*** QBs which have provided adverse information, such as the past due or litigation status of loan accounts, to credit information bureaus, or any organization performing similar functions, shall submit monthly reports to these bureaus or organizations on the full payment or settlement of the previously reported accounts within five (5) business days from the end of the month when such full payment was received. For this purpose, it shall be the responsibility of the reporting QBs to ensure that their disclosure of any information about their borrowers/clients is with the consent of borrowers/clients concerned.

(Circular No. 589 dated 18 December 2007)

Sec. 4307Q ***(2008 - 4309Q)*** **"Truth in Lending Act" Disclosure Requirement** QBs are required to strictly adhere to the provisions of R.A. No. 3765, otherwise known as the "Truth in Lending Act", and shall make the true and effective cost of borrowing an integral part of every loan contract.

The following regulations shall apply to all QBs engaged in the following types of credit transactions:

a. Any loan, mortgage, deed of trust, advance and discount;

b. Any conditional sales contract, any contract to sell, or sale or contract of sale of property or services, either for present or future delivery, under which part or all of the price is payable subsequent to the making of such sale or contract;

c. Any rental-purchase contract;

d. Any contract or arrangement for the hire, bailment, or leasing of property;

e. Any option, demand, lien, pledge, or other claim against, or for delivery of property or money;

f. Any purchase, or other acquisition of, or any credit upon the security of, any obligation or claim arising out of any of the foregoing; and

g. Any transaction or series of transactions having a similar purpose or effect.

The following categories of credit transactions are outside the scope of these regulations:

(1) Credit transactions which do not involve the payment of any finance charge by the debtor; and

(2) Credit transactions in which the debtor is the one specifying a definite and fixed set of credit terms such as bank deposits, insurance contracts, sale of bonds, etc.

§ 4307Q.1 ***(2008 - 4309Q.1) Definition of terms***

a. *Person* means any individual, partnership, corporation, association, or other organized group of persons, or the legal successor or representative of the foregoing, and includes the Philippine Government or any agency thereof, or any other government, or any of its political subdivisions, or any agency of the foregoing.

b. *Cash price or delivered price,* in case of trade transactions, is the amount of money which would constitute full

payment upon delivery of the property (except money) or service purchased at the QB's place of business. In the case of financial transactions, cash price represents the amount of money received by the debtor upon consummation of the credit transaction, net of finance charges collected at the time the credit is extended, if any.

c. *Down payment* represents the amount paid by the debtor at the time of the transaction in partial payment for the property or service purchased.

d. *Trade-in* represents the value of an asset agreed upon by the QB and debtor, given at the time of the transaction as partial payment for the property or service purchased.

e. *Non-finance charges* correspond to the amounts advanced by the QB for items normally associated with the ownership of the property or the availment of the service purchased which are not incidental to the extension of credit. For example, in the case of the purchase of an automobile on credit, the QB may advance the insurance premium as well as the registration fee for the account of the debtor.

f. *Amount to be financed* consists of the cash price plus non-finance charges less the amount of the down payment and value of the trade-in.

g. *Finance charge* represents the amount to be paid by the debtor incidental to the extension of credit such as interest or discount, collection fee, credit investigation fee, attorney's fee and other service charges.

The total finance charge represents the difference between (i) the aggregate consideration (down payment plus installments) on the part of the debtor, and (ii) the sum of the cash price and non-finance charges.

h. *Simple annual rate* is the uniform percentage which represents the ratio, on an annual basis, between the finance charges and amount to be financed.

In the case of single payment upon maturity, the simple annual rate *(R)* in percent is determined by the following method:

$$R = \frac{\text{finance charge}}{\text{amount to be financed}} \times \frac{12}{\text{maturity period in months}} \times 100$$

In the case of the normal installment type of credit of at least one (1) year in duration, where installment payments of equal amount are made in regular time periods spaced not more than one (1) year apart, the *R* in percent is computed by the following method:

$$R = 2 \times \frac{\text{finance charge}}{\text{amount to be financed}} \times \frac{\text{number of payments in a year}}{\text{total number of payments plus one}} \times 100$$

In cases where the credit matures in less than one (1) year (e.g., installment payments are required every month for six (6) months), the same formula will apply except that *number of payments in a year* would refer to the number of installment periods, as defined in the credit contract, as if the credit matures in one (1) year. For example, *number of payments in a year* would be twelve (12) for this purpose in cases where six (6) monthly installment payments are called for in the credit transaction[1]. In cases where credit terms provide for premium or penalty charges depending on, for instance, the timeliness of the debtor's payments, the annual rate to be disclosed in writing shall be the rate for regular payments, i.e., the premium and penalty need not be taken into account in the determination of the annual rate. Such premium or penalty charges shall, however, be indicated in the credit contract.

§ 4307Q.2 ***(2008 - 4309Q.2) Information to be disclosed.*** QBs shall furnish to each person to whom credit is extended, prior to the consummation of the transaction, a clear

[1] This can be determined by dividing twelve, the number of months in a year, by the number or fraction of months between installment payments.

statement in writing setting forth the following information:

a. The cash price or delivered price of the property or service to be acquired;

b. The amounts, if any, to be credited as down payment and/or trade-in;

c. The difference between the amounts set forth under Items *"a"* and *"b"*;

d. The charges, individually itemized, which are paid or to be paid by such person in connection with the transaction but which are not incident to the extension of credit;

e. The total amount to be financed;

f. The finance charges expressed in terms of pesos and centavos; and

g. The percentage that the finance charge bears to the total amount to be financed expressed as a simple annual rate on the outstanding unpaid balance of the obligation.

The contract covering the credit transaction, or any other document to be acknowledged and signed by the debtor, shall indicate the above seven (7) items of information. In addition, the contract or document shall specify additional charges, if any, which will be collected in case certain stipulations in the contract are not met by the debtor.

In case the seven (7) items of information mentioned are not disclosed in the contract covering the credit transaction, all of the items, to the extent applicable, shall be disclosed in another document in the form *(Appendix Q-11)* prescribed by the Monetary Board, to be signed by the debtor and appended to the main contract. A copy of such disclosure statement shall be furnished to the borrower.

§ 4307Q.3 ***(2008 - 4309Q.3) Inspection of contracts covering credit transactions.*** QBs shall keep in their office or place of business copies of contracts which involve the extension of credit and the payment of finance charges therefore. Such copies shall be available for inspection or examination by the appropriate department of the SES.

§ 4307Q.4 ***(2008 - 4309Q.4) Posters*** An abstract of R.A. No. 3765 *(Appendix Q-12)* shall be reproduced in a format sixty (60) cm. wide and seventy-five (75) cm. long and posted on a conspicuous place in the QB's place(s) of business.

Sec. 4308Q (Reserved)

Sec. 4309Q ***(2008 - 4311Q)*** **Non-Performing Loans**

§ 4309Q.1 ***(2008 - 4311Q.1) Accounts considered non-performing; definitions***

a. *Non-performing loans (NPLs)* shall, as a general rule, refer to loan accounts whose principal and/or interest is unpaid for thirty (30) days or more after due date or after they have become past due in accordance with existing rules and regulations. This shall apply to loans payable in lump sum and loans payable in quarterly, semi-annual or annual installments, in which case, the total outstanding balance thereof shall be considered non-performing.

b. In the case of loans payable in monthly installments, the total outstanding balance thereof shall be considered non-performing when three (3) or more installments are in arrears.

c. In the case of loans payable in daily, weekly or semi-monthly installments, the total outstanding balance thereof shall be considered non-performing at the same time that they become past due in accordance with Sec. 4306Q, i.e., the entire outstanding balance of the loan/receivable shall be considered as past due when the total amount of arrearages reaches ten percent (10%) of the total loan/ receivable balance.

d. Restructured loans shall be considered non-performing in accordance with existing rules and regulations.

e. All items in litigation as defined in the Manual of Accounts shall be considered NPLs.

§ 4309Q.2 ***(2008 - 4311Q.2) Interest accrual on past due loans.*** No accrual of interest income is allowed if a loan has become non-performing as defined under Subsec. 4322Q.1. Interest on NPLs shall be taken up as income only when actual payment thereon is received.

Interest income on past due loans arising from discount amortization (and not from the contractual interest of the accounts) shall be accrued as provided in PAS 39.

§ 4309Q.3 ***(2008 - 4311Q.3) Allowance for uncollected interest on loans.*** A contra account to be designated Allowance for Uncollected Interest on Loans shall be set up in accordance with *Appendix Q-10* if accrued interest receivable on loans and loan installments is still uncollected after three (3) months from the date such loans have become non-performing.

§ 4309Q.4 ***(2008 - 4311Q.4) Reporting requirement.*** QBs shall report the following data at the end of each month as additional information in the monthly Consolidated Statement of Condition starting with their report as of 31 May 1999.

Total non-performing loans	xxx
Non -performing regular loans	xxx
Non -performing restructured loan	xxx

Sec. 4310Q - 4313Q *(*Reserved)

B. (RESERVED)

Secs. 4314Q - 4318Q (Reserved)

C. UNSECURED LOANS

Sec. 4319Q *(2008 - 4336Q)* Loans Against Personal Security. The grant, renewal, restructuring or extension of unsecured loans shall, in addition to the requirements of Sec. 4304Q, be made under the signature of the principal borrower and, at least one (1) co-maker, except that a co-maker is not required when the principal borrower has the financial capacity and a good track record of paying his obligations.

(As amended by Circular No. 622 dated 16 September 2008)

§ 4319Q.1 ***(2008 - 4336Q.1) General guidelines***

(Deleted by Circular No. 622 dated 16 September 2008)

§ 4319Q.2 ***(2008 - 4336Q.2) Proof of financial capacity of borrower***

(Deleted by Circular No. 622 dated 16 September 2008)

§ 4319Q.3 ***(2008 - 4336Q.3) Signatories***

(Deleted by Circular No. 622 dated 16 September 2008)

§ 4319Q.4 ***(2008 - 4336Q.4) (Reserved)***

Sec. 4320Q *(2008 - 4337Q)* Credit Card Operations; General Policy. The BSP shall foster the development of consumer credit through innovative products such as credit cards under conditions of fair and sound consumer credit practices. The BSP likewise encourages competition and transparency to ensure more efficient delivery of services and fair dealings with customers.

Towards this end, the following rules and regulations shall govern the credit card operations of QBs and subsidiary/affiliate credit card companies, aligned with global best practices.

§ 4320Q.1 (2008 - 4337Q.1) Definition of terms

a. *Credit card*. Means any card, plate, coupon book or other credit device existing for the purpose of obtaining money, property, labor or services on credit.

b. *Credit card receivables*. Represents the total outstanding balance of credit cardholders arising from purchases of goods and services, cash advances, annual membership/renewal fees as well as interest,

penalties, insurance fees, processing/service fees and other charges.

c. *Minimum amount due* or *minimum payment required*. Means the minimum amount that the credit cardholder needs to pay on or before the payment due date for a particular billing period/cycle as defined under the terms and conditions or reminders stated in the statement of account/billing statement which may include: (1) total outstanding balance multiplied by the required payment percentage or a fixed amount whichever is higher; (2) any amount which is part of any fixed monthly installment that is charged to the card; (3) any amount in excess of the credit line; and (4) all past due amounts, if any.

d. *Default* or *delinquency*. Shall mean non-payment of, or payment of any amount less than, the "*Minimum Amount Due*" or "*Minimum Payment Required*" within two (2) cycle dates, in which case, the "*Total Amount Due*" for the particular billing period as reflected in the monthly statement of account may be considered in default or delinquent.

e. *Acceleration clause*. Shall mean any provision in the contract between the QB and the cardholder that gives the QB the right to demand the obligation in full in case of default or non-payment of any amount due or for whatever valid reason.

f. *Subsidiary* refers to a corporation or firm more than fifty percent (50%) of the outstanding voting stock of which is directly or indirectly owned, controlled or held with the power to vote by a QB or other FI.

g. *Affiliate* refers to an entity linked directly or indirectly to a QB or other FI through any one or a combination of any of the following:

(1) Ownership, control or power to vote, whether by permanent or temporary proxy or voting trust, or other similar contracts, by a QB or other financial institution of at least ten percent (10%) or more of the outstanding voting stock of the entity, or vice-versa;

(2) Interlocking directorship or officership, except in cases involving independent directors as defined under existing regulations;

(3) Common stockholders owning at least ten percent (10%) of the outstanding voting stock of each FI and the entity; or

(4) Management contract or any arrangement granting power to the QB or other FI to direct or cause the direction of management and policies of the entity, or vice-versa.

§ 4320Q.2 ***(2008 - 4337Q.2) Risk management system.*** To safeguard their interests, QBs and subsidiary/affiliate credit card companies are required to establish an appropriate system for managing risk exposures from credit card operations which shall be documented in a complete and concise manner. The risk management system shall cover the organizational set-up, records and reports, accounting, policies and procedures and internal control.

Written policies, procedures and internal control guidelines shall be established on the following aspects of credit card operations:

a. Requirements for application;

b. Solicitation and application processing;

c. Determination and approval of credit limits;

d. Issuance, distribution and activation of cards;

e. Supplementary or extension cards;

f. Cash advances;

g. Billing and payments;

h. Deferred payment program or special installment plans;

i. Collection of past due accounts;

j. Handling of accounts for write-off;

k. Suspension, cancellation and

withdrawal or termination of card;

l. Renewal of cards, upgrade or downgrade of credit limit;

m. Lost or stolen cards and their replacement;

n. Accounts of DOSRI and employees;

o. Disposition of errors and/or questions about the billing statement/ statement of account and other customers' complaints; and

p. Dealings with marketing agents/ collection agents.

(As amended by Circular No. 702 dated 15 December 2010)

§ 4320Q.3 ***(2008 - 4337Q.3) Minimum requirements.*** QBs and their subsidiary or affiliate credit card companies shall not issue pre-approved credit cards.

Before issuing credit cards, QBs and/or their subsidiary/affiliate credit card companies must exercise, in accordance with the provisions of Subsec. 4304Q.1, proper diligence by ascertaining that applicants possess good credit standing and are financially capable of fulfilling their credit commitments.

The net take home pay of applicants who are employed, the net monthly receipts of those engaged in trade or business, or the net worth or cash flow inferred from deposits of those who are neither employed nor engaged in trade or business or the credit behavior exhibited by the applicant from his other existing credit cards, or other lifestyle indicators such as but not limited to club memberships, ownership and location of residence and motor vehicle ownership shall be determined and used as basis for setting credit limits. The gross monthly income may also be used provided reasonable deductions are estimated for income taxes, premium contributions, loan amortizations and other deductions.

All credit card applications, specially those solicited by third party representatives/agents, shall undergo a strict credit risk assessment process and the information stated thereon validated and verified by authorized personnel of the QBs and their subsidiary or affiliate credit card companies, other than those handling marketing.

(As amended by Circular No. 702 dated 15 December 2010)

§ 4320Q.4 ***(2008 - 4337Q.4) Information to be disclosed.*** QBs or their subsidiaries/affiliate credit card companies shall disclose to each person to whom the credit card privilege is extended in the agreement, contract or any equivalent document governing the issuance or use of the credit card or any amendment thereto or in such other statement furnished to the cardholder from time to time, prior to the imposition of the charges and to the extent applicable, the following information:

a. non-finaqnce charges, individually itemized, which are paid or to be paid by the cardholder in connection with the transaction but which are not incident to the extension of credit;

b. the percentage that the interest bears to the total amount to be financed expressed as a simple monthly or annual rate, as the case may be, on the outstanding balance of the obligation;

c. the effective interest rate per annum;

d. for installment loans, the number of installments, amount and due dates or periods of payment schedules to repay the indebtedness;

e. the default, late payment/penalty fees or similar delinquency-related charges payable in the event of late payments;

f. the conditions under which interest may be imposed, including the time period, within which any credit extended may be repaid without interest;

g. the method of determining the balance upon which interest and/or delinquency charges may be imposed;

h. the method of determining the amount of interest and/or delinquency charges, including any minimum or fixed

amount imposed as interest and/or delinquency charge;

i. where one (1) or more periodic rates may be used to compute interest, each such rate, the range of balances to which it is applicable, and the corresponding simple annual rate;

j. other fees, such as membership/ renewal fees, processing fees, collection fees, credit investigation fees and attorney's fees; and

k. for transactions made in foreign currencies and/or outside the Philippines, for dual currency accounts (peso and dollar billings), as well as payments made by credit cardholders in any currency other than the billing currency: the application of payments; the manner of conversion from the transaction currency and payment currency to Philippine pesos or billing currency; definition or general description of verifiable blended exchange/conversion rates (e.g., MASTERCARD and/or VISA International rates on the day the item was processed/posted to the billing statement, plus markup, if any) including conversion commission; and/or other currency conversion charges and costs arising from the purchase by the card company of foreign currency to settle the customer's transactions shall also be disclosed.

QBs and their subsidiary or affiliate credit card companies shall also provide the following information to their cardholders:

1. A table of the applicable fees, penalties and interest rates on credit card transactions, including the period covered by and the manner of and reason for the imposition of such penalties, fees and interests; fees and applicable conversion reference rates for third currency transactions, in plain sight and language, on materials for marketing credit cards, such as brochures, flyers, primers and advertising materials, on credit card application forms, and on credit card billing statements: *Provided,* That these disclosures are in addition to the full disclosure of the fees, charges and interest rates in the terms and conditions of the credit card agreement found elsewhere on the application form and billing statement; and

2. A reminder to the cardholder in the monthly billing statement, or its equivalent document, that payment of only the minimum amount due or any amount less than the total amount due for the billing cycle/period, would mean the imposition of interest and/or other charges:

Provided, That such table of fees, penalties and interest rates and reminder shall be printed in plain language and in bold black letters against a light or white background, and using the minimum Arial 12 theme font and size, or its equivalent in readability, and on the first page, if applicable document has more than one page.

Transitory provisions. QBs and their subsidiary or affiliate credit card companies shall be given a period of 120 days from 06 January 2011 to fully implement the required disclosure requirements.

(As amended by Circular No. 702 dated 15 December 2010)

§ 4320Q.5 ***(2008 - 4337Q.5) Accrual of interest earned.*** Interest accrued and/or booked shall be reversed and no accrual of interest shall be allowed ninety (90) days after the credit card receivable has become past due as defined in Subsec. 4306Q.1.

§ 4320Q.6 ***(2008 - 4337Q.6) Finance charges.*** The amount of finance charges in connection with any credit card transaction shall refer to interest charged to the cardholder.

§ 4320Q.7 ***(2008 - 4337Q.7) Deferral charges.*** The QB and the cardholder may, prior to the consummation of the transaction, agree in writing to a deferral of all or part of one (1) or more unpaid installments and the QB may collect a

deferral charge which shall not exceed the rate previously disclosed pursuant to the provisions on disclosure.

§ 4320Q.8 ***(2008 - 4337Q.8) Late payment/penalty fees.*** No late payment or penalty fee shall be collected from cardholders unless the collection thereof is fully disclosed in the contract between the issuer and the cardholder: *Provided*, That late payment or penalty fees shall be based on the unpaid minimum amount due or a prescribed minimum fixed amount: *Provided, further,* That said late payment or penalty fees may be based on the total outstanding balance of the credit card obligation, including amounts payable under installment terms or deferred payment schemes, if the contract between the issuer and the cardholder contains an "*acceleration clause*" and the total outstanding balance of the credit card is classified and reported as past due.

§ 4320Q.9 ***(2008 - 4337Q.9) Confidentiality of information.*** QBs and subsidiary/affiliate credit card companies shall keep strictly confidential the data on the cardholder or consumer, except under the following circumstances:

a. disclosure of information is with the consent of the cardholder or consumer;

b. release, submission or exchange of customer information with other FIs, credit information bureaus, credit card issuers, their subsidiaries and affiliates;

c. upon orders of court of competent jurisdiction or any government office or agency authorized by law, or under such conditions as may be prescribed by the Monetary Board;

d. disclosure to collection agencies, counsels and other agents of the QB or card company to enforce its rights against the cardholder;

e. disclosure to third party service providers solely for the purpose of assisting or rendering services to the QB or card company in the administration of its credit card business; and

f. disclosure to third parties such as insurance companies, solely for the purpose of insuring the QB from cardholder default or other credit loss, and the cardholder from fraud or unauthorized charges.

§ 4320Q.10 ***(2008 - 4337Q.10) Suspension, termination of effectivity and reactivation.*** QBs or their subsidiary/affiliate credit card companies shall formulate criteria or parameters for suspension, revocation and reactivation of the right to use the card and shall include in their contract with cardholders a provision authorizing the issuer to suspend or terminate its effectivity, if circumstances warrant.

§ 4320Q.11 ***(2008 - 4337Q.11) Inspection of records covering credit card transactions.*** QBs or their subsidiary/affiliate credit card companies shall make available for inspection or examination by the appropriate department of the SES complete and accurate files on card applicant/cardholder to support the consideration for approval of the application and determination of the credit limit which shall be in accordance with the verified debt repayment ability and/or net worth of the card applicant/cardholder.

§ 4320Q.12 ***(2008 - 4337Q.12) Offsets*** For purposes of transparency and adequate disclosure, the credit card issuer shall inform/notify the credit cardholder in the agreement, contract or any equivalent document governing the issuance or use of the credit card that, pursuant to the provisions of Articles 1278 to 1290 of the New Civil Code of the Philippines, as amended the use of his credit card will subject his deposit/s with the QB to offset

against any amount/s due and payable on his credit card which have not been paid in accordance with the terms of the agreement/ contract.

§ 4320Q.13 ***(2008 - 4337Q.13) Handling of complaints.*** QBs or subsidiary/ affiliate credit card companies shall give cardholders at least twenty (20) calendar days from statement date to examine charges posted in his/her statement of account and inform the QB/subsidiary credit card companies in writing of any billing error or discrepancy. Within ten (10) calendar days from receipt of such written notice, the QB/subsidiary credit card company shall send a written acknowledgement to the cardholder unless the action required is taken within such ten (10)-day period.

Not later than two (2) billing cycles or two (2) months which in no case shall exceed ninety (90) days after receipt of the notice and prior to taking any action to collect the contested amount, or any part thereof, QBs/subsidiary credit card companies shall make appropriate corrections in their records and/or send a written explanation or clarification to the cardholder after conducting an investigation. Nothing in this Subsection shall be construed to prohibit any action by the QB/subsidiary credit card company to collect any amount which has not been indicated by the cardholder to contain a billing error or apply against the credit limit of the cardholder the amount indicated to be in error.

§ 4320Q.14 ***(2008 - 4337Q.14) Unfair collection practices.*** QBs, subsidiary/ affiliate credit card companies, collection agencies, counsels and other agents may resort to all reasonable and legally permissible means to collect amounts due them under the credit card agreement: *Provided,* That in the exercise of their rights and performance of duties, they must observe good faith and reasonable conduct and refrain from engaging in unscrupulous or untoward acts. Without limiting the general application of the foregoing, the following conduct is a violation of this Subsection:

a. the use or threat of violence or other criminal means to harm the physical person, reputation, or property of any person;

b. the use of obscenities, insults, or profane language which amount to a criminal act or offense under applicable laws;

c. disclosure of the names of credit cardholders who allegedly refuse to pay debts, except as allowed under Subsec. 4320Q.9;

d. threat to take any action that cannot legally be taken;

e. communicating or threat to communicate to any person credit information which is known to be false, including failure to communicate that a debt is being disputed;

f. any false representation or deceptive means to collect or attempt to collect any debt or to obtain information concerning a cardholder; and

g. making contact at unreasonable/ inconvenient times or hours which shall be defined as contact before 6:00 A.M. or after 10:00 P.M., unless the account is past due for more than sixty (60) days or the cardholder has given express permission or said times are the only reasonable or convenient opportunities for contact.

QBs and their subsidiary/affiliate credit card companies shall inform their cardholders in writing of the endorsement of the collection of their account to a collection agency/agent, or the endorsement of their account from one collection agency/ agent to another, at least seven (7) days prior to the actual endorsement. The notification shall include the full name of the collection agency and its contact details: *Provided*,

That the required notification in writing shall be included in the terms and conditions of the credit card agreement. QBs and their subsidiary/affiliate credit card companies shall adopt policies and procedures to ensure that personnel handling the collection of accounts, whether these are in-house collectors, or third-party collection agents, shall disclose his/her full name/true identity to the cardholder.
(As amended by Circular No. 702 dated 15 December 2010)

§ 4320Q.15 ***(2008-4337Q.15) Sanctions.*** Violations of the provisions of Subsecs. 4320Q.1, 4320Q.5 to 4320Q.13 shall be subject to any or all of the following sanctions depending upon their severity:

a. Disqualification of the QB concerned from the credit facilities of the BSP except as may be allowed under Section 84 of R.A. No. 7653;

b. Prohibition of the QB concerned from the extension of additional credit accommodation against personal security; and

c. Penalties and sanctions provided under Sections 36 and 37 of R.A. No. 7653.

Violations of the provisions of Subsecs. 4320Q.2 to 4320Q.4 and 4320Q.14 shall be subject to any or all of the following sanctions depending upon their severity:

a. *First offense*. Reprimand for the directors/officers responsible for the violation;

b. Second offense. Disqualification of the bank concerned from the credit facilities of the BSP except as may be allowed under Section 84 of R. A. No. 7653;

c. *Subsequent offense/s:*

i. Prohibition on the QB concerned from the extension of additional credit accommodation against personal security; and

ii. Penalties and sanctions provided under Sections 36 and 37 of R. A. No. 7653.
(As amended by Circular No. 702 dated 15 December 2010)

Sec. 4321Q (Reserved)

D. RESTRUCTURED LOANS

Sec. 4322Q *(2008 - 4351Q)* Restructured Loans; General Policy. QBs shall have full discretion in the restructuring of loans in order to provide flexibility in arranging the repayment of such loans without impairing or endangering the lending QB's financial interest, except in special cases approved by the Monetary Board such as loans funded partly or wholly by foreign currency obligations. However, the restructuring of loans granted to DOSRI shall be upon terms not less favorable to the QB than those offered to others. While agreements on loan restructuring should be considered as management tools to maintain or improve the soundness of the QB's lending operations, these should be drawn mainly to assist borrowers towards the settlement of their loan obligations, taking into account their capacity to pay.

§ 4322Q.1 ***(2008 - 4351Q.1) Definition; when to consider performing/ non-performing.*** Restructured loans are loans the principal terms and conditions of which have been modified in accordance with a restructuring agreement setting forth a new plan of payment or a schedule of payment on a periodic basis. The modification may include, but is not limited to, change in maturity, interest rate, collateral or increase in the face amount of the debt resulting from the capitalization of accrued interest/accumulated charges. Items in litigation and loans subject of judicially-approved compromise, as well as those covered by petitions for suspension or for new plans of payment approved by the court or the SEC, shall not be classified as restructured loans.

A loan which is restructured shall be considered non-performing except:

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(1) When the loan is current and performing (i.e., with updated principal and interest payments) on the date of restructuring, in which case, the loan shall retain its performing status; and

(2) Fully secured by real estate with loan value of up to sixty percent (60%) of the appraised value of the real estate security and the insured improvements thereon, and such other first class collaterals as may be deemed appropriate by the Monetary Board: *Provided,* That a restructured loan, with or without capitalized interest, must be yielding a rate of interest equal to or greater than the QB's average cost of funds at the date of restructuring, otherwise, it shall be considered non-performing.

The restoration to a performing loan shall only be effective after a *satisfactory track record* of payments of the required amortizations of principal and/or interest has been established.

For this purpose, a *satisfactory track record* of payments of principal and/or interest shall mean three (3) consecutive payments of the required amortizations of principal and/or interest have been made. However, in the case of a restructured loan with capitalized interest but not fully secured by real estate with loan value of up to sixty percent (60%) of the appraised value of the real estate security and the insured improvements thereon or other first class collaterals, six (6) consecutive payments of the required amortizations of principal and/or interest must have been made.

A restructured loan which has been restored to a performing loan status shall be immediately considered non-performing in case of default of any principal or interest payment in accordance with Sec. 4306Q.

§ 4322Q.2 ***(2008 - 4351Q.2) Procedural requirements***

a. A loan may be restructured subject to the approval of the QB's board of directors in a resolution which shall embody, among other things:

(1) the basis of or justification for the approval;

(2) determination of the borrower's capacity to pay, such as viability of the business; and

(3) the nature and extent of protection of the QB's exposure.

The authority to approve the restructuring of loans may be delegated by the QB's board of directors to a committee or officer(s): *Provided,* That there are board-prescribed guidelines specifically on restructuring of loans: *Provided, further,* That said guidelines shall be submitted to the appropriate department of the SES within thirty (30) days following the date of approval thereof. However, loans previously approved by the executive committee as well as those granted to DOSRI shall be subject to approval by the board as provided under existing rules and regulations. Loans restructured other than those approved by the board shall be reported to it for confirmation.

b. A second restructuring of a loan shall be allowed only if there are reasonable justifications: *Provided* that it shall be considered a non-performing loan and classified, at least, "Substandard". The restoration to a performing loan status and/or the upgrading of loan classification, e.g., from "Substandard" to "Loans Especially Mentioned", if circumstances warrant an upgrading in accordance with the criteria under *Appendix Q-10*, shall only be allowed after a satisfactory track record of at least six (6) consecutive payments of the required amortization of principal and/or interest has been established.

c. In the restructuring process, the QB shall encourage the borrower to improve the quality of the loan either by strengthening financial capacity or providing additional collateral.

The real estate security and/or other first class collaterals offered shall be appraised at the time of restructuring to ensure that

current market values are being used. Real estate security shall be appraised by an independent appraisal company acceptable to the BSP and shall be reappraised every year thereafter.

The term "first class collaterals" refers to assets and securities which have relatively stable and clearly definable value and/or greater liquidity and are free from lien/ encumbrance, such as:

(1) Real estate;

(2) Evidences of indebtedness of the Republic of the Philippines and of the BSP, and other evidences of indebtedness or obligations the servicing and repayment of which are fully guaranteed by the Republic of the Philippines;

(3) Hold-out on and/or assignment of deposit substitutes maintained in the lending institutions;

(4) "Blue chip" shares of stocks, except those issued by the lending entity or by its parent company which owns more than fifty percent (50%) of its outstanding shares of stocks. For this purpose, the issuer corporation must be a listed corporation with a net worth of at least P1.0 billion and with annual net earnings during the immediately preceding five (5) years; and

(5) Such other collaterals that the Monetary Board may declare as first class collaterals from time to time.

It is understood that the loan value to be assigned the collateral shall be as prescribed under existing regulations.

§ 4322Q.3 *(Reserved)*

§ 4322Q.4 *(2008 - 4351Q.3)*

Classification. The classification of a loan prior to restructuring, e.g., "Loans Especially Mentioned", "Substandard" or "Doubtful" shall be retained: *Provided*, That a loan that is not classified but which is non-performing prior to restructuring shall be classified, at least, "Loans Especially Mentioned": *Provided, further,* That restructured loans with capitalized interest shall be classified, at least, "Substandard" and the required valuation reserves shall be set up accordingly: *Provided*, *finally*, That a more adverse classification may be given, i.e., "Substandard", "Doubtful" or "Loss", if the circumstances warrant it as provided under *Appendix Q-10*.

The upgrading of loan classification, e.g., from "Substandard" to "Loans Especially Mentioned", if circumstances warrant an upgrading in accordance with the criteria in *Appendix Q-10,* shall only be effective after a satisfactory track record of payments of the required amortizations of principal and/or interest has been established.

For this purpose, a *satisfactory track record* of payments of principal and/or interest shall mean three (3) consecutive payments of the required amortizations of principal and/or interest have been made. However, in the case of a restructured loan with capitalized interest but not fully secured by real estate with loan value of up to sixty percent (60%) of the appraised value of the real estate security and the insured improvements thereon or other first class collaterals, six (6) consecutive payments of the required amortizations of principal and/or interest must have been made.

Secs. 4323Q - 4325Q (Reserved)

E. LOANS/CREDIT ACCOMMODATIONS TO DIRECTORS, OFFICERS, STOCKHOLDERS AND THEIR RELATED INTERESTS

Sec. 4326Q *(2008 - 4356Q)* General Policy. Dealings of a QB with any of its DOSRI shall be in the regular course of business and upon terms not less favorable to the QB than those offered to others.

No QB shall grant, renew or extend any credit accommodation to its DOSRI whenever its combined capital accounts is deficient relative to risk assets held under Sec. 4115Q, or whenever its paid-in capital is deficient relative to the required minimum capitalization. Neither shall it grant, renew or extend any credit accommodation to any of its DOSRI who has past due credit accommodations with the QB.

§ 4326Q.1 ***(2008 - 4356Q.1) Definitions.*** For purposes of these regulations, the following definitions shall apply.

a. *Directors* shall refer to QB directors as defined in Sec. 4141Q.

b. *Officers* shall refer to QB officers as defined in Sec. 4142Q.

c. *Stockholder* shall refer to any stockholder of record in the books of the QB/trust entity, acting personally, or through an attorney-in-fact; or any other person duly authorized by him or through a trustee designated pursuant to a proxy or voting trust or other similar contracts, whose stockholdings in the lending QB/trust entity, individual and/or collectively with the stockholdings of: (i) his spouse and/or relative within the first degree by consanguinity or affinity or legal adoption; (ii) a partnership in which the stockholder and/or the spouse and/or any of the aforementioned relatives is a general partner; and (iii) corporation, association or firm of which the stockholder and/or his spouse and/or the aforementioned relatives own more than fifty percent (50%) of the total subscribed capital stock of such corporation, association or firm, amount to one percent (1%) or more of the total subscribed capital stock of the QB/trust entity.

d. *Outstanding loans to and placements with the QB* shall refer to loans to and deposit substitutes of the QB which are not subject of an assignment or hold-out agreement.

e. *Book value of the paid-in capital contribution* shall mean the proportional amount of the QB's total capital accounts (net of such unbooked valuation reserves and other capital adjustments as may be required by the BSP) as the corresponding paid-in capital contribution of each director, officer or stockholder concerned bears to the total paid-in capital of the QB: *Provided,* That as a basis for determining the individual ceiling referred to in Sec. 4330Q, corresponding book value of the shares of stock of such director, officer or stockholder which are the subject of pledge, assignment or any other encumbrance shall be deducted therefrom.

f. *Secured loan, borrowing, or credit accommodation* shall refer to any loan, discount, credit or advance, or portion thereof referred to in Sec. 4327Q which is secured by real estate mortgage, chattel mortgage on tangible assets, standby letters of credit issued by foreign banks, assignments of or hold-out on deposit substitutes issued by the lending entity, cash margin deposits, assignment or pledge of government securities or readily marketable bonds and other highgrade debt securities except those issued by the lending entity, or by its parent company which owns more than fifty percent (50%) of its outstanding shares of stocks, or receivables arising from financial leases to the extent of the guaranty deposit plus sixty percent (60%) of the remaining value of the leased equipment. For this purpose, the remaining value of the equipment under lease shall be determined by dividing the acquisition cost by the original term of the lease and multiplying the resulting ratio by the unexpired portion of the term.

For investment houses with quasi-banking functions, a secured loan, borrowing or credit accommodation shall likewise include:

(1) Customer's liability under import bills outstanding for not more than thirty (30) days from date of original entry;

(2) Sales contract receivable arising out of sale of real property on credit wherein title to the property is retained by the QB; and

(3) Customer's liability-import bills under trust receipts outstanding for not more than thirty (30) days from date of booking: *Provided,* That the booking under trust receipts shall have been made not later than the thirty-first (31st) day from the date of original entry referred to in Sub-item *(1)* above.

g. *Unsecured loan, borrowing or credit accommodation* shall refer to any loan, discount, credit or advance, or portion thereof referred to in Sec. 4327Q which is not secured in accordance with Item *"f"* above.

Sec. 4327Q *(2008 - 4357)* Transactions Covered. The terms *loan, borrow, money borrowed* and *credit accommodations* as used herein shall refer to transactions which involve the grant, renewal, extension or increase of any loan, discount, credit or advance in any form whatsoever, and shall include:

a. Outstanding availments under an established credit line;

b. Drawings against an existing letter of credit;

c. The acquisition by discount, purchase, exchange or otherwise of any note, draft, bill of exchange or other evidence of indebtedness upon which a director, officer or stockholder may be liable as a maker, drawer, acceptor, endorser, guarantor, or surety;

d. Any advance of unearned salary or unearned compensation for periods in excess of thirty (30) days;

e. Loans or other credit accommodations granted by another FI to such director, officer or stockholder from funds of the QB invested in the other institution's trust or other department when there is a clear relationship between the transactions;

f. The increase of an existing indebtedness, as well as additional availments under a credit line or additional drawings against a letter of credit;

g. The sale of assets, such as shares of stock, on credit;

h. Leasing transactions under R.A. No. 5980, as amended; and

i. Any other transaction as a result of which a director, officer or stockholder becomes obligated or may become obligated to the lending QB, directly or indirectly, by any means whatsoever to pay money or its equivalent.

Sec. 4328Q *(2008 - 4358Q)* Transactions Not Covered. The terms *loan, borrow, money borrowed or credit accommodation* as used herein shall not refer to the following transactions:

a. Advances against accrued compensation, or for the purpose of providing payment of authorized travel, legitimate expenses or other transactions for the account of the QB or for utilization of maternity and other leave credits;

b. The increase in the amount of outstanding credit accommodation as a result of additional charges or advances made by the QB to protect its interests such as taxes, insurance, etc.;

c. The discount of bills of exchange drawn in good faith against actually existing values, and the discount of commercial or business paper actually owned by the person negotiating the same, including, but not limited to, the acquisition of export bills from any of its DOSRI which are drawn in accordance with the terms and conditions of the covering letters of credit: *Provided,* That the transaction shall automatically be subject to the ceiling as herein provided once the DOSRI who is a party to the transaction becomes directly liable to the QB;

d. Transactions with a foreign bank or other FI which has stockholding in the QB

where the foreign bank or other FI acts as guarantor through the issuance of letters of credit, guarantee letters or assignment of a deposit in a currency eligible as part of the international reserves and held in a bank in the Philippines to secure credit accommodations granted to another person or entity: *Provided,* That the foreign bank stockholder shall automatically be subject to the ceilings as herein provided in the event that its contingent liability as guarantor becomes a real liability; and

e. Deposits of a QB with a bank, whether domestic or foreign, which has stockholdings in the QB.

§ 4328Q.1 ***(2008 - 4358Q.1) Applicability to credit card operations.*** The credit card operations of QBs shall not be subject to these regulations where the credit cardholder is a director, officer or stockholder of the QB or their related interests (DOSRI): *Provided*, That (a) the privilege of becoming a credit cardholder is open to all qualified persons on the basis of selective criteria which are applied by the QB to all applicants thereof; and (b) the director, officer or stockholder/related interest concerned reimburses/pays the QB for the billed amount in full on or before the payment due date in the billing or statement of account, as set by the QB for all other qualified credit cardholders on availments made for the same period on their credit cards. However, the transaction shall be subject to applicable DOSRI regulations if the director, officer, or stockholder/ related interest concerned:

a. fails to reimburse/pay the QB within the period mentioned herein; or

b. on the outset, opts for deferred payment scheme, and the availment is booked by the QB.

Sec. 4328Q.2 - 4328Q.4 ***(Reserved)***

§ 4328Q.5 ***(2008 - 4328Q) Loans, other credit accommodations and guarantees granted to subsidiaries and/or affiliates***

a. *Statement of policy*. Dealings of a QB with its subsidiaries and/or affiliates shall be in the regular course of business and upon terms not less favorable to the institution than those offered to others.

b. *Ceilings*. The total outstanding loans, other credit accommodations and guarantees to each of the QB's subsidiaries and affiliates shall not exceed ten percent (10%) of the net worth of the lending QB: *Provided*, That the unsecured loans, other credit accommodations and guarantees to each of said subsidiaries and affiliates shall not exceed five percent (5%) of such net worth: *Provided, further*, That the total outstanding loans, other credit accommodations and guarantees to all subsidiaries and affiliates shall not exceed twenty percent (20%) of the net worth of the lending QB: *Provided, finally,* That these subsidiaries and affiliates are not related interest of any of the director, officer, and/ or stockholder of the lending institution, except where such director, officer or stockholder sits in the board of directors or is appointed officer of such corporation as representative of the QB.

Loans, other credit accommodations and guarantees granted by a QB to its subsidiaries and affiliates engaged in energy and power generation consistent with the medium-term Philippine development plan/ medium-term public investment program of the National Government duly certified as such by the secretary of the socio-economic planning shall be subject to a separate individual limit of twenty-five percent (25%) of the net worth of the lending QB: *Provided*, That the unsecured portion thereof shall not exceed twelve and one-half percent (12.5%) of such net worth: *Provided, further*, That these subsidiaries and affiliates are not related interests of any of the director,

officer, and/or stockholder of the lending QB, except where such director, officer or stockholder sits in the board of directors or is appointed officer of such corporation as representative of the QB.

c. *Exclusions from the ceilings*. Loans, other credit accommodations and guarantees secured by assets considered as non-risk under existing BSP regulations as well as interbank call loans shall be excluded in determining compliance with the ceilings prescribed under Item *"b"* above.

d. *Procedural requirements*. The following provisions shall apply if a QB grants a loan, other credit accommodation or guarantee to any of its subsidiaries and affiliates.

(1) *Approval of the board, when to obtain*. Except with prior written approval of the majority of all the members of the board of directors, no loan, other credit accommodation and guarantee shall be granted to a subsidiary or affiliate.

(2) *Approval by the board, how manifested*. The approval shall be manifested in a resolution passed by the board of directors during a meeting and made of record.

(3) *Determination of majority of all the members of the board of directors*. The determination of the majority of all the members of the board of directors shall be based on the total number of directors of the QB as provided in its articles of incorporation and by-laws.

(4) *Contents of the resolution*. The resolution of the board of directors shall contain the following information:

(a) Name of the subsidiary or affiliate;

(b) Nature of the loan or other credit accommodation or guarantee, purpose, amount, credit basis for such loan or other credit accommodation or guarantee, security and appraisal thereof, maturity, interest rate, schedule of repayment and other terms;

(c) Date of resolution;

(d) Names of the directors who participated in the deliberation of the meeting; and

(e) Names in print and signatures of the directors approving the resolution: *Provided*, That in instances where a director who participated in the board meeting and who approved such resolution failed to sign, the corporate secretary may issue a certification to this effect indicating the reason for the failure of the said director to sign the resolution.

(5) *Transmittal of copy of board approval; contents thereof*. A copy of the written approval of the board of directors, as herein required, shall be submitted to the appropriate department of the SES within twenty (20) business days from the date of approval. The copy may be a duplicate of the original, or a reproduction copy showing clearly the signatures of the approving directors: *Provided*, That if a reproduction copy is to be submitted, it shall be duly certified by the corporate secretary that it is a reproduction of the original written approval.

e. *Reportorial requirements*. Each QB shall maintain a record of loans, other credit accommodations and guarantees covered by these regulations in a manner and form that will facilitate verification of such transactions by BSP examiners.

The appropriate department of the SES may require QBs to furnish such data or information as may be necessary for purposes of implementing the provisions of the foregoing rules.

f. *Sanctions*. Without prejudice to the criminal sanctions under Section 36 of R.A. No. 7653 (The New Central Bank Act), any violation of the provisions of the foregoing rules shall be subject to any or all of the following sanctions:

(1) Restriction or prohibition on the QB from declaring dividends for non-compliance with the herein prescribed

ceilings until the outstanding loans, other credit accommodations and guarantees have been reduced to within the herein prescribed ceilings;

(2) For the duration of each violation, imposition of a fine of one tenth (1/10) of one percent (1%) of the excess over the ceilings per day but not to exceed P30,000 a day on the following:

(a) The lending QB;

(b) Each of the directors voting for the approval of the loan, other credit accommodation or guarantee in excess of any of the ceilings prescribed above.

g. *Transitory provisions*. Outstanding loans, other credit accommodation and guarantees to subsidiaries/affiliates that will exceed the ceilings mentioned above shall not be subject to penalty until 09 April 2007 or until said accommodations become past due, or are extended, renewed or restructured, whichever comes later.

(Circular No. 560 dated 31 January 2007, as amended by 654 dated 12 May 2009)

(Next page is Part III - Page 27)

Sec. 4329Q *(2008 - 4359Q)* Direct or Indirect Borrowings. For purposes of this Section, a credit accommodation shall be considered a direct or indirect borrowing in accordance with the following criteria.

a. *Direct borrowing* - If the director, officer or stockholder of the lending QB is a party to any of the transactions enumerated in Sec. 4327Q for himself or as a representative or agent of others, or if he acts as a guarantor, endorser or surety for loans from the QB, or if the loan or credit accommodation to another party is secured by a property interest or right of the director, officer or stockholder.

b. *Indirect borrowing* - If in any of the transactions in Sec. 4327Q the borrower, guarantor, indorser, or surety is a:

(1) Spouse or relative within the first degree of consanguinity or affinity, or relative by legal adoption of a director, officer or stockholder of the QB;

(2) Partnership of which a director, officer, or stockholder or his spouse or relative within the first degree of consanguinity or affinity, or relative by legal adoption, is a general partner;

(3) Co-owner with the director, officer, stockholder or his spouse or relative within the first degree of consanguinity or affinity, or relative by legal adoption, of the property or interest or right mortgaged, pledged or assigned to secure the loans or credit accommodations, except when the mortgage, pledge or assignment covers only said co-owner's undivided interest;

(4) Corporation, association, or firm of which a director or officer of the QB, or his spouse is also a director or officer of such corporation, association or firm, except (i) where the securities of such corporation, association or firm are listed and traded in the domestic stock exchange and less than fifty percent (50%) of the voting stock thereof is owned by any one (1) person or by persons related to each other within the third degree of consanguinity or affinity; or (ii) where the director, officer or stockholder of the lending QB sits as a representative of the QB in the board of directors of such corporation: *Provided,* That the QB representative shall not have any equity interest in the borrower corporation except for the minimum shares required by law, rules and regulations, or by the by-laws of the corporation, to qualify a person as director of the corporation: *Provided, further,* That the borrowing corporation under *(i)* or *(ii)* is not among those mentioned in Items *"b(5)"* and *"b(6)"* of this Section;

(5) Corporation, association or firm of which any or a group of directors, officers, stockholders of the lending QB and/or their spouses or relatives within the first degree of consanguinity or affinity or relative by legal adoption, hold/own more than twenty percent (20%) of the subscribed capital of such corporation, or of the equity of such association or firm; or

(6) Corporation, association or firm wholly or majority-owned or controlled by any or a group of related entities mentioned in Items *"b(2)", "b(4)"* and *"b(5)"* of this Section.

Other cases of direct/indirect borrowing shall be resolved on a case-to-case basis.

It shall be the responsibility of the QB concerned to ascertain whether the borrower, guarantor, representative, endorser or surety is related to persons mentioned in Item *"b(1)"* of this Section or connected with any of the directors, officers or stockholders of the QB in any of the capacities mentioned in Items *"b(2)", "b(3)", "b(4)", "b(5)"* and *"b(6)"* of this Section.

In determining indirect borrowings as enumerated above, only those cases involving living relatives shall be considered.

Sec. 4330Q *(2008 - 4360Q)* Individual Ceiling; Single- Borrower Limit. The total outstanding direct credit accommodations to each of the QB's directors, officers or stockholders, excluding those granted under officers' fringe benefit plans, shall not exceed, at any time, an amount equivalent to the unencumbered portion of his loans to, and placements with, the QB and the book value of his paid-in capital contribution in the lending QB: *Provided,* That unsecured credit accommodations to each of the QB's directors, officers or stockholders shall not exceed thirty percent (30%) of his total credit accommodations.

Notwithstanding the provisions of this Section, credit accommodations of a QB to any one of its directors, officers, stockholders or their related interests shall not exceed the SBL prescribed for QBs.

Sec. 4331Q *(2008 - 4361Q)* Aggregate Ceiling; Ceiling On Unsecured Loans. Except with prior approval of the Monetary Board, the total outstanding borrowings of directors, officers, or stockholders, whether direct or indirect,shall not exceed 100% of combined capital accounts, net of deferred income tax as defined in Item *"i"* of Subsec. 4116Q.2 and such unbooked valuation reserves and other capital adjustments as may be required by the BSP: *Provided,* That in no case shall the total unsecured direct and indirect borrowings of directors, officers, and stockholders exceed thirty percent (30%) of the aggregate ceiling or the outstanding direct/ indirect loans thereto, whichever is lower. For the purpose of determining compliance with the ceiling on unsecured loans, QBs shall be allowed to average their ceiling on unsecured loans and their outstanding unsecured loans every week.

In evaluating requests for extension of loans in excess of the aggregate ceiling, the BSP shall consider the credit standing of the borrower, viability of the projects financed by such loans in relation to national objectives, collateral or security and other pertinent considerations.

Sec. 4332Q *(2008 - 4362Q)* Exclusions from Aggregate Ceiling. The following credit accommodations shall be excluded in determining compliance with the aggregate ceiling:

a. Credit accommodations to the extent covered by a hold-out on, or assignment of, deposit substitutes in the lending QB, or covered by cash margin deposits or secured by evidences of indebtedness of the Republic of the Philippines or of the Bangko Sentral, or by other evidences of indebtedness or obligations, the servicing and repayment of which are fully guaranteed by the Republic of the Philippines;

b. Credit accommodations to a corporate stockholder which meets all the following conditions:

(1) The corporation is a non-financial institution;

(2) Its shares are listed and traded in the domestic stock exchanges;

(3) Its stockholdings in the lending QB do not exceed thirty percent (30%) of the voting stock of the QB; and

(4) No person or group of persons related within the first degree of consanguinity or affinity holds/owns more than twenty percent (20%) of the subscribed capital of the corporation; and

c. Credit accommodations granted under officers' fringe benefit plans.

Sec. 4333Q *(2008 - 4363Q)* Credit Accommodations Under Officers' Fringe Benefit Plans. The aggregate outstanding liabilities to a QB of its officers, extended under officers' fringe benefit plans for the

purpose of house, car, and appliance financing, and meeting educational, medical, hospital, and other similar expenses, shall not exceed thirty percent (30%) of the combined capital accounts of the lending entity: *Provided,* That QBs shall submit, for record purposes, copies of their officers' fringe benefit plans to the appropriate department of the BSP.

Sec. 4334Q *(2008 - 4364Q)* Procedural Requirements. The following provisions shall apply if a director or officer is a party, directly or indirectly, to, or acts as the representative or agent of, others in any of the transactions under Sec. 4327Q.

a. *Approval of the board of directors; when to obtain*. Except with the prior written approval of the majority of the directors, excluding the director concerned, no loan or other credit accommodation shall be granted nor any of the transactions under Sec. 4327Q be entered into.

b. *Approval by the board; how manifested*. The approval shall be manifested in a resolution passed by the board of directors duly assembled during a regular or special meeting for the purpose and made of record.

c. *Majority of the directors; computation of*. The computation of the majority of the directors, excluding the director concerned, shall be based on the total number of directors of the QB, as provided in its articles of incorporation and by-laws.

d. *Contents of the resolution*. The resolution of the board of directors shall contain the following information:

(1) Name of the director or officer concerned and his relationship as regards the credit accommodation, such as principal, endorser, spouse of borrower, etc.;

(2) Nature of the loan or other credit accommodation, purpose, amount, credit basis for such loan or credit accommodation, security and appraisal thereof, maturity, interest rate, schedule of repayment, and other terms of the loan or credit accommodation;

(3) Date of the resolution;

(4) Names of the directors who were present and who participated in the deliberations of the meeting;

(5) Names in print and signatures of the directors approving the resolution: *Provided,* That the corporate secretary may sign, under a power-of-attorney, in behalf of a director who was present in the board meeting and who approved such resolution, in instances where such signature is necessary, to indicate that such resolution was approved by a majority of the directors; and

(6) Such other information as may be required by the appropriate department of the SES.

e. *Transmittal of copy of board of directors' approval; contents thereof*. A copy of the written approval of the board of directors, as herein required, shall be submitted to the appropriate department of the SES within twenty (20) business days from the date of approval. The copy may be a duplicate of the original, or a reproduction copy showing clearly the signatures of the approving directors: *Provided,* That if a reproduction copy is to be submitted, it shall contain, on its face or reverse side, a signed certification by the secretary that it is a reproduction of the original written approval.

Sec. 4335Q (Reserved)

Sec. 4336Q *(2008 - 4365Q)* Sanctions. Any violation of the provisions of the foregoing rules shall be subject to any or all of the following sanctions:

a. Restriction or prohibition on the QB from declaring dividends until the outstanding loans and other credit

accommodations have been reduced to within the herein prescribed ceilings;

b. Disqualification of the directors voting for the approval of the loan or credit in excess of any of the ceilings prescribed in Secs. 4330Q and 4331Q from participating in the approval of loans or credit to officers, directors, and stockholders of the QB: *Provided, however,* That the disqualification may be lifted by the BSP, as the circumstances warrant;

c. Application of (1) the borrowing director's or officer's share in the QB's profit sharing program and (2) the share of the director voting for the approval of the loan or credit accommodation against the excess of such loan or credit accommodation over any of the herein prescribed ceilings for such period of time as may be approved by the Monetary Board; and

d. For the duration of each violation, imposition of a fine of one-tenth of one percent (1/10 of 1%) of the excess over the ceilings per day but not to exceed P30,000 a day on (1) the lending QB and the director, officer, or stockholder whose borrowing exceeds his individual ceiling and (2) each of the directors voting for the approval of the loan or credit accommodation in excess of any of the ceilings prescribed in Secs. 4330Q and 4331Q.

The penalty for exceeding the individual ceiling, aggregate ceiling and ceiling on unsecured loans shall be computed on the average amount of loans in excess of said ceilings during the same week.

Secs. 4337Q - 4339Q (Reserved)

Sec. 4340Q *(2008 - 4366Q)* Bank DOSRI Rules and Regulations Applicable to Government Borrowings in Government-Owned or - Controlled Quasi-Banks. The provisions of Secs. X326 to X337 of the Manual of Regulations for Banks (MORB), to the extent applicable, shall also apply to loans, other credit accommodations, and guarantees granted to the National Government or Republic of the Philippines, its political subdivisions and instrumentalities as well as GOCCs, subject to the following clarifications:

a. Loans, other credit accommodations, and guarantees to the Republic of the Philippines and/or its agencies/departments/bureaus shall be considered: (1) non-risk; and (2) not subject to any ceiling;

b. Loans, other credit accommodations, and/or guarantees to: (1) GOCCs; and (2) corporations where the Republic of the Philippines, its agencies/departments/bureaus, and/or GOCCs own at least twenty percent (20%) of the subscribed capital stock shall be considered indirect borrowings of the Republic of the Philippines and shall form part of the individual ceiling as well as the aggregate ceiling: *Provided,* That the following loans, other credit accommodations, and/or guarantees to GOCCs and corporations where the Republic of the Philippines, its agencies/departments/bureaus, and/or GOCCs own at least twenty percent (20%) of the subscribed capital stock, shall be excluded from the thirty percent (30%) ceiling on unsecured loans under Secs. X330 and X331 of the MORB:

(1) Loans, other credit accommodations, and/or guarantees for the purpose of undertaking priority infrastructure projects consistent with the Medium-Term Development Plan/Medium-Term Public Investment Program of the National Government, duly certified as such by the Secretary of Socio-Economic Planning;

(2) Loans, other credit accommodations, and/or guarantees granted to participating financial institutions (PFIs) in the lending programs of the government wherein the funds borrowed are intended for relending to other PFIs or end-user borrowers; and

(3) Loans, other credit accommodations, and/or guarantees granted for the purpose of providing (i) wholesale and retail loans

to the agricultural sector, and micro, small and medium enterprises (MSMEs); and/or (ii) rediscounting and guarantee facilities for loans granted to the said sector or enterprises.

c. Loans, other credit accommodations, and/or guarantees granted to state universities and colleges (SUCs) shall be excluded from the thirty percent (30%) ceiling on unsecured loans under Secs. X330 and X331 of the MORB.

d. In view of the fiscal autonomy granted under R.A. No. 7653 and the independence prescribed under the Constitution, the BSP shall be considered an independent entity, hence, not a related interest of the Republic of the Philippines and/or its agencies/departments/bureaus. Loans, other credit accommodations and guarantees of the BSP shall be considered: (1) non-risk; and (2) not subject to any ceiling;

e. LGUs shall be considered separate from the Republic of the Philippines, other government entities, and from one another due to the full autonomy in the exercise of their proprietary functions and in the management of their economic enterprises granted to them under the Local Government Code of the Philippines, subject to certain limitations provided by law, hence, not a related interest of the Republic of the Philippines and/or its agencies/departments/bureaus;

f. Local Water Districts (LWDs), although GOCCs, shall be considered separate from the Republic of the Philippines, other government entities, and from one another due to their fiscal independence from the national government, hence, not related interests of the Republic of the Philippines and/or its agencies/department/bureaus, for purposes of these regulations;

g. A director who acts as a government representative in the lending institution shall not be excluded in the deliberation as well as in the determination of majority of the directors in cases of loans, other credit accommodations, and guarantees to the Republic of the Philippines and/or its agencies/departments/bureaus; and

h. A director of the lending institution shall be excluded in the deliberation as well as in the determination of majority of the directors in cases of loans, other credit accommodations, and guarantees to the borrowing government entity other than the Republic of the Philippines, its agencies, departments or bureaus where said director is also a director, officer or stockholder under existing DOSRI regulations.

(Circular No. 514 dated 06 March 2006 as amended by Circular Nos. 635 dated 10 November 2008, 616 dated 30 July 2008, 580 dated 09 September 2007)

F. (RESERVED)

Secs. 4341Q - 4342Q (Reserved)

G. SPECIAL TYPES OF LOANS

Sec. 4343Q *(2008 - 4376Q)* Interbank Loans. Interbank loan transactions shall include, among other things, (a) interbank call loan (IBCL) transactions; (b) interbank term loan transactions; (c) borrowings evidenced by deposit substitute instruments; and (d) purchases of receivables with recourse: *Provided, however,* That only IBCL transactions which are settled through the QBs' respective DDAs with the BSP via PhilPaSS shall be eligible to zero percent (0%) reserve requirement: *Provided, further*, That funds borrowed by QBs from trust departments of banks/investment houses shall be excluded from the herein definition of interbank loan transactions.

(As amended by Circular No. 703 dated 23 December 2010 and 689 dated 16 June 2010)

§ 4343Q.1 ***(2008 - 4376Q.1) Systems and procedures for interbank call loan transactions.*** IBCL transactions of QBs shall be governed by the Agreement for the PhilPaSS executed between the BSP and the Investment Houses Association of the Philippines (IHAP) on 12 December 2002 and any subsequent amendments thereto.

(As superseded by the agreement between the BSP and IHAP dated 12 December 2002)

§ 4343Q.2 ***(2008 - 4376Q.2) Accounting procedures***

a. Both lending and borrowing QBs shall immediately pass the corresponding entries in their books.

b. IBCL transactions shall be recorded by the lending QB as *Interbank Call Loans Receivable* and by the borrowing QB as *Bills Payable -Interbank Call Loans Payable*.

c. QBs shall reconcile their DDAs with the BSP against monthly statements of account to be furnished by the BSP Financial Accounting Department Comptrollership Sub-Sector.

(As amended by Circular No. 689 dated 16 June 2010)

§ 4343Q.3 ***(2008 - 4376Q.4) Settlement procedures.*** Interbank loan transactions (call and term) among QBs shall be settled in accordance with the provisions of the Agreement for the PhilPaSS executed between the BSP and the IHAP on 12 December 2002 and any subsequent amendments thereto.

(As superseded by the agreement between the BSP and IHAP dated 12 December 2002)

§ 4343Q.4 ***(2008 - 4376Q.3) Transfer of excess funds.*** The prescribed "Authority to Debit Slip" shall be used by QBs in the transfer of their excess funds which are not otherwise lent out in the interbank loan market from their BSP reserve accounts to their operating accounts with their depository banks.

The "Authority to Debit Slip" shall have a standard size of 4 3/4" x 8 1/2" and shall be orange in color. It shall contain the minimum data or information as required and shall be accomplished and submitted to the BSP Comptrollership Department in duplicate after having been duly signed and/or authenticated by authorized officers of the QB.

Secs. 4344Q - 4380Q (Reserved)

H. EQUITY INVESTMENTS

Sec. 4381Q Investment in Non-Allied Undertakings. In order to avoid undue concentration of economic power, the total equity investments in any single non-allied enterprise or industry of QBs, UBs and their subsidiaries, whether or not the parent financial intermediaries have equity investments in the enterprise, shall, in any case, remain a minority in that enterprise, except as may be otherwise approved by the President of the Philippines. Non-allied enterprises are those allowed for UBs in the MORB.

Equity investments as of 01 April 1980, which exceed the limitation under this Section, may be retained but shall not be increased percentage-wise, and whenever reduced, shall not thereafter be increased beyond the prescribed limitation.

Sec. 4382Q Investments Abroad. Except as may be authorized by the Monetary Board, the total equity investments in and/or loans to any single enterprise abroad by any QB shall not at any time exceed fifteen percent (15%) of the net worth of the investing QB.

Sec. 4383Q Underwriting Exempted. The limitations on equity investments under Sec. 4381Q shall not apply to inventories of equity securities arising out of firm underwriting commitments of investment houses: *Provided,* That such equity holding shall be disposed of within two (2) years from acquisition by the investment house.

I. (RESERVED)

Secs. 4384Q - 4387Q (Reserved)

J. OTHER OPERATIONS

Sec. 4388Q *(2008 - 4391Q)* Purchase of Receivables and Other Obligations. The following rules shall govern the purchase of receivables and other obligations.

§ 4388Q.1 *(2008 - 4391Q.1) Yield on purchase of receivables.* The rate of yield, including commissions, premiums, fees and other charges from the purchase of receivables and other obligations, regardless of maturity, that may be charged or received by QBs shall not be subject to any regulatory ceiling.

Receivables and other obligations shall include claims collectible in money of any amount and maturity from domestic and foreign sources. The Monetary Board shall determine in doubtful cases whether a particular claim is included within said phrase.

§ 4388Q.2 *(Reserved)*

§ 4388Q.3 *(2008 - 4391Q.2) Purchase of commercial paper.* Before purchasing registered commercial paper, QBs shall:

a. Require the issuing entity to submit a duly certified true copy of its Certificate of Registration and Authority to Issue Commercial Paper; and

b. Ascertain that the registration number and expiry date indicated in the commercial paper are the same as those in the Certificate of Registration submitted.

No QB shall sell, discount, assign, negotiate, in whole or in part such as thru syndications, participations and other similar arrangements, any note, receivable, loan, debt instrument and any type of financial asset or claim, except government securities, on a without recourse basis, or be a party in any capacity in any such transactions on a without recourse basis, unless such receivable, note, loan, debt instrument and financial asset or claim is registered with the SEC. This prohibition includes transactions between an investment house and its trust department.

Unregistered commercial papers may be sold, discounted, assigned or negotiated by QBs to other financial intermediaries with quasi-banking functions.

Any violation of the above rules and regulations shall be subject to any or all of the following sanctions:

a. Suspension of quasi-banking authority for a period of six (6) months; and

b. Monetary penalty of P500 per day per transaction for each and every officer of the QB involved in any capacity in any transaction violative of these regulations.

§ 4388Q.4 *(2008 - 4392Q) Reverse Repurchase Agreements with the Bangko Sentral.* Reverse repo agreements may be effected with the BSP under its open market operations, subject to the terms and conditions in Subsec. 4601Q.2.

§ 4388Q.5 *(2008 - 4391Q.3) Investments in debt and marketable equity securities* The classification, accounting procedures, valuation, sales and transfers of investments in debt securities and marketable equity securities shall be in accordance with the guidelines in *Appendices Q-20* and *Q-20-a*.

Penalties and sanctions. The following penalties and sanctions shall be imposed on FIs and concerned officers found to violate the provisions of these regulations:

a. Fines of P2,000/day to be imposed on NBFIs for each violation, reckoned from the date the violation was committed up to the date it was corrected; and

b. Sanctions to be imposed on concerned officers:

(1) First offense – reprimand the officers responsible for the violation; and

(2) Subsequent offenses – suspension of ninety (90) days without pay for officers responsible for the violation

(As amended by Circular Nos. 670 dated 18 November 2009, 628 dated 31 October 2008, 626 dated 23 October 2008 and 585 dated 15 October 2007, M-2007-006 dated 28 February 2007, Circular Nos. 558 dated 22 January 2007, 546 dated 17 November 2006 and 509 dated 01 February 2006)

Secs. 4389Q - 4393Q (Reserved)

Sec. 4394Q Acquired Assets in Settlement of Loans. The following rules shall govern assets acquired in settlement of loans.

§ 4394Q.1 ***(Reserved)***

§ 4394Q.2 ***(2008 - 4394Q.1) Booking***

a. ROPA in settlement of loans through foreclosure or dation in payment shall be booked under the ROPA account as follows:

(1) Upon entry of judgment in case of judicial foreclosure;

(2) Upon execution of the Sheriff's Certificate of Sale in case of extrajudicial foreclosure; and

(3) Upon notarization of the Deed of Dacion in case of dation in payment (*dacion en pago*). ROPA shall be booked initially at the carrying amount of the loan (i.e., outstanding loan balance adjusted for any unamortized premium or discount less allowance for credit losses computed based on PAS 39 provisioning requirements, which take into account the fair value of the collateral) plus booked accrued interest less allowance for credit losses (computed based on PAS 39 provisioning requirements) plus transaction costs incurred upon acquisition (such as non-refundable capital gains tax and documentary stamp tax paid in connection with the foreclosure/ purchase of the acquired real estate property): *Provided,* That if the carrying amount of ROPA exceeds P5.0 million, the appraisal of the foreclosed/purchased asset shall be conducted by an independent appraiser acceptable to the BSP.

b. The carrying amount of ROPA shall be allocated to land, building, other non-financial assets and financial assets (e.g., receivables from third party or equity interest in an entity) based on their fair values, which allocated carrying amounts shall become their initial costs.

c. The non-financial assets portion of ROPA shall remain in ROPA and shall be accounted for as follows:

(1) Land and buildings shall be accounted for using the cost model under PAS 40 "Investment Property";

(2) Other non-financial assets shall be accounted for using the cost model under PAS 16 "Property Plant and Equipment";

(3) Buildings and other non-financial assets shall be depreciated over the remaining useful life of the assets, which shall not exceed ten (10) years and three (3) years from the date of acquisition, respectively; and

(4) Land, buildings and other non-financial assets shall be subject to the impairment provisions of PAS 36 "Impairment".

d. Financial assets, shall be reclassified and booked according to intention under HFT, DFVPL, AFS, HTM, INMES, Unquoted Debt Securities Classified as Loans or Loans and Receivable and accounted for in accordance with the provisions of PAS 39, except interests in subsidiaries, associates and joint ventures, which shall be booked under Equity

Investments in Subsidiaries, Associates and Joint Ventures and accounted for in accordance with the provisions of PAS 27, 28 and 31, respectively.

e. ROPAs that comply with the provisions of PFRS 5 "Non-Current Assets Held for Sale" shall be reclassified and accounted for as such.

f. Claims arising from deficiency judgments rendered in connection with the foreclosure of mortgaged properties shall be lodged under the real account "Deficiency Judgment Receivable"; while probable claims against the borrower arising from the foreclosure of mortgaged properties shall be lodged under the contingent account "Deficiency Claims Receivable".

g. *Appraisal of properties*. Before foreclosing or acquiring any property in settlement of loans, it must be properly appraised to determine its true economic value. If the amount of ROPA to be booked exceeds P5.0 million, the appraisal must be conducted by an independent appraiser acceptable to the BSP. An in-house appraisal of all ROPAs shall be made at least every other year: *Provided,* That immediate re-appraisal shall be conducted on ROPAs which materially decline in value.

h. *Non-cash payment for interest* FIs that accept non-cash payments for interest on their borrowers' loans shall book the acquired assets as ROPA. The amount to be booked as ROPA shall be the booked accrued interest less allowance for credit losses (computed based on PAS 39 provisioning requirements): *Provided,* That if the carrying amount of ROPA exceeds P5.0 million, the appraisal of the foreclosed/ purchased asset shall be conducted by an independent appraiser acceptable to the BSP. The carrying amount of ROPA shall be allocated in accordance with Item *"b"* and shall be subsequently accounted for in accordance with Item *"c"* of this Subsection.

The provisions of this Subsection shall be applied retroactively to all outstanding ROPAs and sales contract receivables: *Provided:* That for properties acquired before 01 January 2005, the carrying amount of the acquired properties when initially booked under ROPA shall be the cost subject to depreciation and impairment testing, which shall be reckoned from the time of acquisition.

(As amended by Circular Nos. 555 dated 12 January 2007 and 520 dated 20 March 2006)

§ 4394Q.3 *(2008 - 4394Q.2) Sales contract receivable*

a. Sales Contract Receivable (SCR) shall be recorded based on the present value of the installment receivables discounted at the imputed rate of interest. Discount shall be accreted over the life of the SCR by crediting interest income using the effective interest method. Any difference between the present value of the SCR and the derecognized assets shall be recognized in profit or loss at the date of sale in accordance with the provisions of PAS 18 "Revenue" *Provided, furthermore*, That SCR shall be subject to impairment provision of PAS 39.

The provisions of this Section shall be applied retroactively to all outstanding ROPAs and SCRs: *Provided:* That for properties acquired before 01 January 2005, the carrying amount of the acquired properties when initially booked under ROPA shall be the cost subject to depreciation and impairment testing, which shall be reckoned from the time of acquisition.

b. SCRs which meet all the requirements/conditions enumerated below are hereby considered performing assets and therefore, not subject to classification:

(1) That there has been a down-payment of at least twenty percent (20%)

of the agreed selling price or in the absence thereof, the installment payments on the principal had already amounted to at least twenty percent (20%) of the agreed selling price;

(2) That payment of the principal must be in equal installments or in diminishing amounts and with maximum intervals of one (1) year;

(3) That any grace period in the payment of principal shall not be more than two (2) years; and

(4) That there is no installment payment in arrear either on principal or interest. *Provided,* That a "*Sales Contract Receivable*" account shall be automatically classified "*Substandard*" and considered non-performing in case of non-payment of any amortization due: *Provided, further*, That a *"Sales Contract Receivable"* which has been classified "*Substandard*" and considered non-performing due to non-payment of any amortization due may only be upgraded/restored to unclassified and/or performing status after a satisfactory track record of at least three (3) consecutive payments of the required amortization of principal and/or interest has been established.

(As amended by Circular No. 520 dated 20 March 2006)

§§ 4394Q.4 - 4394Q.9 *(Reserved)*

§ 4394Q.10 *(2008 - 4396Q) Transfer/ Sale of non-performing assets to a special purpose vehicle or to an individual.* The procedures governing the transfer/sale of non-performing assets (NPAs) to a Special Purpose Vehicle (SPV) or to an individual that involves a single family residential unit, or transactions involving *dacion en pago* by the borrower or third party of a non-performing loan (NPL), for the purpose of obtaining the Certificate of Eligibility (COE) which is required to avail of the incentives provided under R.A. No. 9182 are presented in *Appendix Q-28*.

The accounting guidelines on the sale of NPAs to SPVs and to qualified individuals for housing under the SPV Act of 2002 are presented in *Appendix Q-28-a*.

The significant timelines relative to the implementation of R.A. No. 9182, also known as the "Special Purpose Vehicle Act", as amended by R.A. No. 9343 are presented in *Appendix Q-28b*.

(As amended by M-2008-014 dated 17 March 2008, M-2008-005 dated 04 February 2008, M-2007-013 dated 11 May 2007 and M-2006-001 dated 11 May 2006)

§§ 4394Q.11 - 4394Q.14 *(Reserved)*

§§ 4394Q.15 *Joint venture of quasi-banks with real estate development companies*

a. *Statement of policy*. It is the policy of the BSP to encourage QBs to dispose of their ROPA in settlement of loans and other advances either through foreclosure or *dacion en pago* as well as other properties acquired as a consequence of a merger/ consolidation which are no longer necessary for their quasi-banking operations. Towards this end, QBs are hereby authorized to enter into Joint Venture Agreements (JVA) with real estate development companies for the development of said properties, subject to the requirements prescribed under this Subsection.

b. For purposes of this Subsection, *joint venture* shall refer to a contractual arrangement/undertaking between a QB and a duly registered real estate development company (developer) for the purpose of developing the above-mentioned properties of the QB. The QB contributes said properties to the undertaking while the developer contributes all the development funds, resources, technical expertise, equipment, personnel and all other requirements desired or needed for the implementation

and completion of the undertaking including marketing, where applicable. The QB and the developer shall be bound by the contract that establishes joint control of the undertaking. Although the developer may be designated as operator or manager of the undertaking, it does not, however, absolutely control the undertaking but only acts in accordance with the authorities granted to him under the JVA.

c. *Forms of a joint venture*. A QB and a developer may undertake a joint venture under the following forms:

(1) A jointly-controlled operation/ undertaking, which does not involve the establishment of a corporation, partnership or other entity, or a financial structure that is separate from the QB and the developer themselves. Under this form of joint venture, the rights and obligations of the QB and the developer shall be governed primarily by their contract that must clearly specify the following:

(a) authority of the developer to develop/subdivide the property and subsequently, to sell the individual lots under a special power of attorney;

(b) sharing in the sales proceeds of the developed ROPAs or in the developed lots;

(c) sharing in taxes;

(d) sharing in the assets of the joint venture particularly in the developed/ subdivided lots should there still be unsold lots at the time of termination of the joint venture; and

(e) name under which the subdivided lots shall be registered pending their sale.

(2) A jointly-controlled entity, which involves the establishment of a new juridical entity, preferably a corporation that is separate and distinct from the QB and the developer. A jointly controlled corporation may be established either for the purpose of developing properties of QBs for immediate sale or converting them into earning assets such as hotels and shopping malls.

d. *Requirements and limitations in a joint venture*. A QB desiring to enter into a JVA with a developer for the purpose of developing its ROPAs and/or other properties acquired as a consequence of merger/consolidation shall comply with the following:

(1) The JVA shall be approved by the board of directors of the QB.

(2) The QB's contribution to the joint venture, in whatever form undertaken, shall be limited to ROPAs and properties acquired as a consequence of the QB's merger/consolidation with another QB/FI.

(3) The QB shall not recognize income out of its contribution to the joint venture, regardless of the agreed valuation of said properties.

(4) The QB shall not provide funds to the joint venture either as a loan or capital contribution.

(5) The JVA or contractual arrangement shall clearly stipulate the rights and obligations of the QB and the developer.

(6) The QB shall secure prior Monetary Board approval of the JVA.

e. *Application for authority to enter into JVA*. A QB desiring to enter into a JVA with a developer for the purpose of developing its ROPAs and other properties acquired as a consequence of its merger/ consolidation with another QB/FI shall secure prior Monetary Board approval of said agreement. For that purpose, the concerned QB shall submit an application for Monetary Board approval to the appropriate department of the SES. The application shall be signed by the QB's president or officer of equivalent rank and shall be accompanied by the following documents/information:

(1) The name of the developer;

(2) Name of the principal stockholders and officers as well as members of the board of directors of said company;

(3) Relationship of the QB with the developer, if any;

(4) List and brief description of the properties to be contributed by the QB including their market values, book values and the valuation agreed upon under the proposed JVA;

(5) Certification by the QB's president or officer of equivalent rank that the JVA is strictly in compliance or will strictly comply with the requirements of this Subsection; and

(6) Such other documents/information that the concerned department of the SES may require.

f. *Non-financial allied undertaking* All types of QBs are hereby authorized to invest in the equities of companies engaged in real estate development as a non-financial allied undertaking, subject to the following conditions:

(1) Investments shall be limited to ROPAs and other properties acquired as a consequence of a QB's merger/ consolidation with another QB/FI;

(2) Investments shall be subject to existing BSP requirements applicable to investments in non-financial allied undertakings; and

(3) If there is already an existing subsidiary or affiliate relationship between the QB and the investee corporation prior to the investment, the QB shall not recognize income out of its invested properties. The excess of the value of the capital stock received by the QB over the book value of its invested properties shall be booked as "Deferred Credits".

g. *Accounting treatment*. Accounting treatment of the properties contributed by a QB to a joint venture or invested in the equities of developers.

(1) In a joint venture in the form of a jointly controlled operations/undertaking, which does not involve the establishment of a corporation or other entity, the QB shall continue to recognize in its books the properties contributed to the undertaking. However, the regular provisioning against probable losses required under existing regulations may be discontinued upon execution and implementation of the JVA.

(2) In a joint venture in which a corporation is created, the QB shall book the properties contributed to the undertaking as investment pursuant to the provisions of PAS 31. It shall also recognize its interest in the corporation using the proportionate consolidation method or the equity method as long as it continues to have joint control over the corporation: *Provided,* That the QB shall not recognize income out of its contribution to the joint venture. The excess of the value of the capital stock received by the QB over the book value of the contributed properties shall be credited to the account "Deferred Credits".

(3) Properties invested in equities of developers shall be booked in accordance with the PAS: *Provided,* That the QB shall not recognize income out of the properties invested if there is already an existing subsidiary or affiliate relationship between the QB and the investee corporation prior to the investment, regardless of the agreed valuation of said properties. The excess of the agreed valuation of said properties over their book value shall be booked as "Deferred Credits".

h. *Coverage*. The provisions of this Subsection shall apply to ROPAs existing, as well as those which may be acquired by QBs in settlement of non-performing or past due loans and advances outstanding, as of 09 March 2006 and to properties acquired as a consequence of merger or consolidation which are outstanding in the books of QBs as of said date.

i. *Sanctions*. Any violation of the provisions of this Subsection and/or any

misrepresentation in the certification and information required to be submitted to the BSP under this Subsection shall subject the QB and the officer or officers responsible therefore, to the penalties provided under Sections 35, 36 and 37 of R. A. No. 7653.

(Circular No. 518 dated 09 March 2006)

K. MISCELLANEOUS PROVISIONS

Secs. 4395Q - 4398Q (Reserved)

L. GENERAL PROVISION ON SANCTIONS

Sec. 4399Q General Provision on Sanctions. Unless otherwise provided for, any violation of the provisions of this Part shall be subject to Sections 36 and 37 of R.A. No. 7653.

The guidelines for the imposition of monetary penalty for violations/offenses with sanctions falling under Section 37 of R. A. No. 7653 on QBs, their directors and/or officers are shown in *Appendix Q-39*.

PART FOUR

TRUST, OTHER FIDUCIARY BUSINESS AND INVESTMENT MANAGEMENT ACTIVITIES

Section 4401Q Statement of Principles The cardinal principle common to all trust and other fiduciary relationships is fidelity. Policies predicated upon this principle are directed towards confidentiality, scrupulous care, safety and prudent management of property including reasonable probability of income with proper accounting and appropriate reporting thereon. Practices are designed in accordance with the basic standards for trust, other fiduciary and investment management accounts (IMAs) in *Appendix Q-48* to promote efficiency in administration and operation; to adhere and conform to the terms of the instrument or contract; and to maintain absolute separation of property free from any intrusion of conflict of interest.

An institution incorporated or authorized to engage in trust and fiduciary business is under no obligation, either legal or moral, to accept any such business being offered nor has it the right to accept if the same is contrary to law, rules, regulations, public order and public policy. It shall advertise its services in a dignified manner and enter such business only when demand for such service is evident, when specially equipped to render such service and upon full appreciation of the responsibilities involved. It shall be ready and willing to give full disclosure of the services being offered and shall conduct its dealing with transparency. Harmonious relationship shall likewise be pursued with other professions to achieve the common goal of mutual service to the public and protection of its interest.

(As amended by Circular No. 618 dated 20 August 2008)

Sec. 4402Q Scope of Regulations. These regulations shall govern the grant of authority to and the management, administration and conduct of *trust, other fiduciary business and investment management activities* (as these terms are defined in Sec. 4403Q) of NBFIs (e.g., investment houses (IHs) and trust corporations) allowed by law to perform such operations.

The regulations are divided into three (3) Sub-Parts where:

A. *Trust and Other Fiduciary Business* shall apply to institutions authorized to engage in trust and other fiduciary business including investment management activities;

B. *Investment Management Activities* shall apply to institutions without trust authority but engaged in investment management activities; and

C. *General Provisions* shall apply to both.

Sec. 4403Q Definitions. For purposes of regulating the operations of trust and other fiduciary business and investment management activities, unless the context clearly connotes otherwise, the following shall have the meaning indicated.

a. *Trust business* shall refer to any activity resulting from a trustor-trustee relationship (trusteeship) involving the appointment of a trustee by a trustor for the administration, holding, management of funds and/or properties of the trustor by the trustee for the use, benefit or advantage of the trustor or of others called beneficiaries.

b. *Other fiduciary business* shall refer to any activity of trust-licensed institutions resulting from a contract or agreement whereby the institution binds itself to render services or to act in a representative capacity such as in an agency, guardianship, administratorship of wills, properties and estates, executorship, receivership and other similar services which do not create or result in a trusteeship. It shall exclude collecting or paying agency arrangements and similar fiduciary services which are inherent in the use of the facilities of the other operating departments of such institution. Investment management activities, which are considered as among other fiduciary business, shall be separately defined in the succeeding item to highlight its being a major source of fiduciary business.

c. *Investment management activity* shall refer to any activity resulting from a contract or agreement primarily for financial return whereby the institution (the investment manager) binds itself to handle or manage investible funds or any investment portfolio in a representative capacity as financial or managing agent, adviser, consultant or administrator of financial or investment management, advisory, consultancy or any similar arrangement which does not create or result in a trusteeship.

d. *Trust* is a relationship or an arrangement whereby a person called a trustee is appointed by a person called a trustor to administer, hold and manage funds and/or property of the trustor for the benefit of a beneficiary.

e. *Trust agreement* is an instrument in writing covering the terms and conditions of the trust.

f. *Trustee* is any person who holds legal title to the funds and/or property of a trust.

g. *Trustor* is any person who creates a trust.

h. *Beneficiary* is any person for whose benefit a trust is created.

i. *Fiduciary* shall refer to any person or entity engaged in any of the other fiduciary business as herein defined where no trustor-trustee relation exists.

j. *Agency* shall refer to a contract whereby a person binds himself to render some service or to do something in representation or on behalf of another, with the consent or authority of the latter.

k. *Principal* shall refer to the person who grants authority to another person called an agent, under a contract to enter into transactions in his behalf.

l. *Agent* shall refer to a person who acts in representation or on behalf of another person with the latter's authority.

m. *Trust Department* shall refer to the department, office, unit, group, division or any aggrupation which carries out the trust and other fiduciary business of an institution.

n. *Trust Officer* shall refer to the designated head or officer-in-charge of the trust department.

o. *Trust account* shall refer to an account where transactions arising from a trusteeship are kept and recorded.

p. *Common Trust Fund (CTF)* shall refer to a fund maintained by an institution authorized to perform trust functions under a written and formally established plan, exclusively for the collective investment and reinvestment of certain money representing participations in the plan received by it in its capacity as the trustee.

q. *Fiduciary account* shall refer to an account where transactions arising from any of the other fiduciary businesses are kept and recorded.

r. *Investment Manager* shall refer to any person or entity engaged in investment management activities as herein defined.

s. *Investment Management Department* shall refer to the department, unit, group, division or any aggrupation

which carries out the investment management activities of an institution that does not have an authority to engage in trust and other fiduciary business.

t. *Investment Management Officer* shall refer to the designated head or officer-in-charge of the investment management department of an institution which does not have the authority to engage in trust and other fiduciary business.

u. *Investment management account* shall refer to an account where transactions arising from investment management activities are kept and recorded.

A. TRUST AND OTHER FIDUCIARY BUSINESS

Sec. 4404Q Authority to Perform Trust and Other Fiduciary Business. With prior approval of the Monetary Board, trust corporations and IHs may engage in trust and other fiduciary business under Chapter IX of R.A. No. 8791, as amended and Section 7 of P.D. No. 129, as amended.

Entities whose articles of incorporation[1] or any amendments thereto, include the purpose or power to engage in trust and other fiduciary business, shall secure the prior favorable recommendation of the Monetary Board pursuant to Section 17 of the Corporation Code.

If an entity is found to be engaged in unauthorized trust and other fiduciary business and/or investment management activities, whether as its primary, secondary or incidental business, the Monetary Board may impose administrative sanctions against such entity or its principal officers and/or majority stockholders or proceed against them in accordance with law.

The Monetary Board may take such action as it may deem proper such as, but may not be limited to, requiring the transfer or turnover of any trust and other fiduciary and/or IMA to duly incorporated and licensed entities of the choice of the trustor, beneficiary or client, as the case may be.

No entity shall advertise or represent itself as being engaged in trust and other fiduciary business or in investment management activities or represent itself as trustee or investment manager or use words of similar import and/or use in connection with its business title, the words *trust*, *trust corporation*, *trust company*, *trust plan* or words of similar import, without having obtained the required authority to do so.

Starting year 2001, IHs authorized to engage in trust and other fiduciary business shall renew their existing licenses yearly, subject to the implementing guidelines to be issued thereon.

(As amended by CL-2008-078 dated 15 December 2008, CL-2008-053 dated 21 August 2008 and CL-2008-007 dated 21 January 2008)

§§ 4404Q.1 - 4404Q.2 *(Reserved)*

§ 4404Q.3 *Prerequisites for engaging in trust and other fiduciary business.* An institution, before it may engage in trust and other fiduciary business, shall comply with the following requirements:

a. The applicant has combined capital accounts of not less than ₱250 million or such amount as may be required by the Monetary Board or other regulatory agency. For this purpose, *combined capital accounts* shall have the same meaning as in Sec. 4111Q;

b. The applicant has been duly licensed or incorporated as an FI by the appropriate government agency or created by special law or charter;

c. The articles of incorporation or charter of the institution shall include among its powers or purposes, acting as trustee or administering any trust or holding

[1] SEC Memorandum Circular Nos. 5 dated 17 July 2008, 3 dated 16 February 2006 and 14 dated 24 October 2000.

property in trust or on deposit for the use, or in behalf of others;

d. The by-laws of the institution shall include, among other things, provisions on the following:

(1) The organization plan or structure of the department, office, or unit which shall conduct the trust and other fiduciary business;

(2) The creation of a trust committee, the appointment of a trust officer and subordinate officers of the trust department; and

(3) A clear definition of the duties and responsibilities as well as the line and staff functional relationships of the various units, officers and staff within the organization.

e. Where the applicant is authorized to engage in quasi-banking functions, it shall also meet the following additional requirements:

(1) Its operations during the year immediately preceding the filing of the application have been profitable, i.e., its rate of return on equity is at least ten percent (10%);

(2) It has continuously complied with its net worth-to-risk assets ratio, liquidity floor and ceilings on DOSRI loans during the last six (6) months immediately preceding the date of application;

(3) It has not incurred net weekly reserve deficiency against deposit substitutes during the last six (6) months immediately preceding the date of application;

(4) The ratio of its total NPLs to its gross loan portfolio as of the date of filing of application does not exceed the industry average as of the end of the quarter immediately preceding the date of application;

(5) It does not have any past due obligation with the BSP or with any government or non-government FI;

(6) It has not engaged in unsafe and unsound practice/s during the year immediately preceding the date of application;

(7) It has corrected as of the date of application the violations noted in its latest examination related to the single borrower's loan limit and all other ceilings prescribed by the BSP;

(8) It does not have float items outstanding for more than sixty (60) calendar days in the "Due From/To Head Office/Branches" accounts and the "Due from Bangko Sentral" account exceeding one percent (1%) of its total resources as of the end of the month immediately preceding the date of application; and

(9) It has shown substantial compliance with other pertinent laws, rules and regulations, policies and instructions of the BSP and it has not been cited for serious violations or exceptions affecting its solvency, liquidity and profitability.

Where the applicant is not authorized to engage in quasi-banking functions:

(i) The adoption of a formula or criteria for QBs in the determination of compliance with the capital-to-risk assets ratio and ceilings on loans to DOSRI; and

(ii) The substitution of the reserve and liquidity floor requirements with the cash ratio, as follows:

(a) Primary reserves to Bills Payable; and

(b) Primary and secondary reserves to Bills Payable; where primary reserves consist of cash on hand, cash in vault, COCIs, due from the BSP and due from banks; and where secondary reserves consist of BSP supported government securities, T-Bills and other government securities.

Compliance with the foregoing, as well as with other requirements under existing regulations, shall be maintained up to the time the trust license is granted. An applicant that fails in this respect shall be required to show compliance for another test period of the same duration.

§ 4404Q.4 ***(2008 - 4404Q.2) Pre-operating requirements.*** An institution authorized to engage in trust and other fiduciary business shall, before engaging in actual operations, submit to the BSP the following:

a. Government securities acceptable to the BSP amounting to P500,000 as minimum basic security deposit for the faithful performance of trust and other fiduciary duties required under Subsec. 4405Q.1;

b. Organization chart of the trust department which shall carry out the trust and other fiduciary business of the institution; and

c. Names and positions of individuals designated as chairman and members of the trust committee, trust officer and other subordinate officers of the trust department with their respective bio-data and statement of duties and responsibilities.

Sec. 4405Q Security for the Faithful Performance of Trust and Other Fiduciary Business

§ 4405Q.1 ***Basic security deposit.*** An institution authorized to engage in trust and other fiduciary business shall deposit with the BSP eligible government securities as security for the faithful performance of its trust and other fiduciary duties equivalent to at least one percent (1%) of the book value of the total volume of trust, other fiduciary and investment management assets: *Provided,* That at no time shall such deposit be less than ₱500,000.

Scripless securities under Registry of Scripless Securities (RoSS) system of the Bureau of Treasury (BTr) may be used as basic security deposit for trust duties using the guidelines in *Appendix Q-21*.

§ 4405Q.2 ***Eligible securities*** Government securities which shall be deposited in compliance with the above basic security deposit shall consist of:

a. Evidences of indebtedness of the Republic of the Philippines and of the BSP and any other evidences of indebtedness or obligations the servicing and repayment of which are fully guaranteed by the Republic of the Philippines; and such other kinds of securities which may be declared eligible by the Monetary Board: *Provided,* That such securities shall be free, unencumbered, and not utilized for any other purpose: *Provided, further,* That such securities shall have remaining maturities of not more than three (3) years from the date of deposit with the BSP;

b. NDC Agri-Agra ERAP Bonds, regardless of remaining maturities;

c. Five (5) - and Ten (10) - year Special Purpose Treasury Bonds (SPTBs) provided such bonds shall not be hypothecated in any way or earmarked for any other purpose and they meet the three (3)-year remaining maturity requirement to ensure that such bonds are liquid;

d. Securities backed by the unreleased Internal Revenue Allotments (IRA) of LGUs (issued by a Special Purpose Trust administered by the DBP under the IRA Monetization Program of the Union of Local Authorities of the Philippines) the release of which IRA on scheduled date of payment has been certified by the DBM as not being subject to any conditionalities: *Provided*, That such securities shall be eligible only to the extent of the present value of the bond computed using the original yield to maturity (as of auction/ issue date): *Provided, further,* That for reserve for trust and other fiduciary duties, the remaining maturities of the securities shall not exceed three (3) years; and

e. Zero Coupon Bond Issue by the HGC of up to ₱7.0 billion five (5)-year regular series and up to ₱3.0 billion seven (7)-year special series to finance its guaranty servicing of socialized and low-cost housing projects: *Provided*, That they meet the three (3)-year remaining maturity

requirement to ensure that such bonds are liquid: *Provided, further,* That such bonds shall qualify as eligible reserve for trust and other fiduciary duties only to the extent of the present value of the bond computed using the original yield to maturity (as of auction/issue date).

f. Tobacco Excise Tax Receivable Monetization Program Investment Certificates (TEXTR Certificates) backed by receivables representing the unreleased portion of the obligation of the National Government to its LGUs for their share of the Tobacco Excise Taxes under R.A. No. 7171 amounting to ₱1.85 billion and covering the years 2001 and 2002: *Provided*, That such securities shall be eligible only to the extent of the present value of the securities computed using the original yield to maturity as of auction/issue date.

g. Securities received, pursuant to the Domestic Debt Exchange Offer of the Republic of the Philippines, in exchange for securities that are eligible reserves for trust duties.

(As amended by Circular No. 509 dated 01 February 2006)

§ 4405Q.3 ***Valuation of securities and basis of computation of the basic security deposit requirement.*** For purposes of determining compliance with the basic security deposit under this Section, the amount of securities so deposited shall be based on their book value, that is, cost as increased or decreased by the corresponding discount or premium amortization.

The base amount for the basic security deposit shall be the average of the month-end balances of total trust, investment management and other fiduciary assets of the immediately preceding calendar quarter.

§ 4405Q.4 ***Compliance period; sanctions.*** The trustee or fiduciary shall have thirty (30) calendar days after the end of every calendar quarter within which to deposit with the BSP the securities required under this Section.

The following sanctions shall be imposed for any deficiency in the basic security deposit for the faithful performance of trust and other fiduciary duties:

a. On the QB:

i. Monetary penalty/ies:

Penalty per Calendar Day	Trust Asset Size \ Offense	First	Second	Third and subsequent offense(s)
QBs with Full Trust Authority and with Trust Assets of	Up to P500 million	P600.00	P700.00	P800.00
	Above P500 million but not exceeding P1 billion	P1,000.00	P1,250.00	P1,500.00
	Above P1 billion but not exceeding P10 billion	P2,000.00	P3,000.00	P4,000.00
	Above P10 billion but not exceeding P50 billion	P5,000.00	P6,000.00	P7,000.00
	Above P50 billion	P8,000.00	P9,000.00	P10,000.00

ii. Non-monetary penalty beginning with the third offense (all QBs) - Prohibition against the acceptance of new trust and other fiduciary accounts, and from renewing expiring trust and other fiduciary contracts up to the time the violation is corrected.

b. On the trust officer and/or other officer(s) responsible for the deficiency/ non-compliance:

(1) *First offense* - warning that subsequent violations shall be dealt with more severely;

(2) *Second offense* - written reprimand with a stern warning that subsequent violations shall be subject to suspension;

(3) *Third offense* - thirty (30) calendar day-suspension without pay; and

(4) *Subsequent offense(s)* - sixty (60) calendar day-suspension without pay.

For purposes of determining the frequency of the violation, the QB's compliance profile for the immediately preceding three (3) years or twelve (12) quarters will be reviewed: *Provided*, That for purposes of determining appropriate penalty on the trust officer and/or other responsible officer(s), any offense committed outside the preceding three (3) year or twelve (12) quarter-period shall be considered as the first offense: *Provided, further*, That in the case of trust officer, all offenses committed by him in the past as trust officer of other institution(s) shall also be considered: *Provided, finally,* That if the offense cannot be attributed to any other officer of the QB, the trust officer shall be automatically held responsible since the ultimate responsibility for ensuring compliance with the regulation rests upon him, as evidence may warrant.

(As amended by Circular Nos. 617 dated 30 July 2008 and 585 dated 15 October 2007)

§ 4405Q.5 *Reserves against peso-denominated Common Trust Funds (CTFs) and Trust and Other Fiduciary Accounts (TOFA) - Others*

a. *Reserves against peso-denominated CTFs*. In addition to the basic security deposit, an institution authorized to engage in trust and other fiduciary business shall maintain reserves on -

(1) peso-denominated CTF; and

(2) such other managed peso funds which partake the nature of collective investment of a peso-denominated CTF as may be indicated by the presence of the following features:

(a) The funds are composed of contributions from two (2) or more investors;

(b) The funds are managed/administered as a vehicle for collective investment and reinvestment;

(c) The trustee/administrator/agent has the exclusive management and control over the funds and the sole right at any time to sell, convert, invest, exchange, transfer or otherwise change or dispose of the assets comprising the funds; and

(d) Investments/contributions to, or withdrawals from, the funds are being allowed at anytime or as of a fixed date in the future, and/or the income, net of all expenses incurred in the management of the fund plus the fee of the trustee/ administrator/agent, are being distributed among the participants of the funds, without the need to liquidate all assets of the funds.

The reserves to be maintained shall be as follows:

(i) Regular reserves 10%[1]

(ii) Liquidity reserves 11%[2]

The liquidity reserve shall be maintained in the RDA with the BSP, or may be in the form of the following: *Provided,* That it complies with the guidelines shown in *Appendix Q-41*.

(i) Short-term market-yielding government securities purchased directly from the BSP-Treasury Department (TD);

(ii) NDC Agri-Agra ERAP Bonds, regardless of maturity. The requirement that the securities used shall have a term of not more than one (1) year shall not apply; and

(iii) Poverty Eradication and Alleviation Certificates (PEACe) bonds only to the extent of the original gross issue proceeds determined at the time of the auction, plus capitalized interest on the underlying zero-coupon Treasury Notes as and when the corresponding interest is earned over the life of the bonds.

[1] From 6% to 9% regular reserve effective the reserve week starting 7 January 2005 under MAB dated 29 December 2004 and from 9% to 10% regular reserve effective the reserve week starting 15 July 2005 under Circular 491 dated 12 July 2005

[2] From 10 % to 11% under Circular 491 dated 12 July 2005, effective the reserve week starting 15 July 2005.

Any defiency in the liquidity reserves shall continue to be in the forms or modes prescribed under existing regulations for the composition of required reserves.

The reserves on peso-denominated CTFs and such other managed peso funds shall be provided out of said funds.

b. *Reserves against TOFA-Others*. In addition to the basic security deposit, an institution authorized to engage in trust and other fiduciary business shall maintain reserves on TOFA-Others, except accounts held under *(1) Administratorship; (2) Bond Issues/Other Obligations Under Deed of Trust or Mortgage; (3) Custodianship and Safekeeping; (4) Depository and Reorganization; (5) Employee Benefit Plans Under Trust; (6) Escrow; (7) Personal Trust (testementary and living trust); (8) Executorship; (9) Guardianship; (10) Life Insurance Trust; and (11) Pre-need Plans (institutional/individual)*.

The reserves to be maintained shall be as follows:

(i) Regular reserves 6%[1]
(ii) Liquidity reserves 11%[2]

The liquidity reserves shall be maintained in the RDA with the BSP, or may be in the form of the following: *Provided,* That it complies with the guidelines shown in *Appendix Q-41*.

(i) Short-term market-yielding government securities purchased directly from the BSP-TD.

(ii) NDC Agri-Agra ERAP Bonds, regardless of maturity; and

(iii) PEACe bonds only to the extent of the original gross issue proceeds determined at the time of the auction, plus capitalized interest on the underlying zero-coupon Treasury Notes as and when the corresponding interest is earned over the life of the bonds.

Any deficiency in the liquidity reserves shall continue to be in the forms or modes prescribed under existing regulations for the composition of required reserves.

The reserves on TOFA-Others shall be provided by the institution out of said funds.
(As amended by Circular Nos. 551 dated 17 November 2006 and 539 dated 09 August 2006)

§ 4405Q.6 *Composition of reserves*

a. The provisions of Section 4254Q shall govern the composition of reserves against peso-denominated CTFs and such other managed peso funds as well as TOFA-Others of institutions authorized to engage in trust and other fiduciary business.

For purposes of this Subsection, a special deposit account shall be maintained by the institutions with the BSP exclusively for trust reserves which deposits up to forty percent (40%) of the required reserves against peso-denominated CTFs and such other managed peso funds (less the percentage allowed to be maintained in the form of short-term market-yielding government securities), as well as the required reserves against TOFA-Others (less the percentage allowed to be maintained in the form of short-term market-yielding government securities), shall be paid interest at four percent (4%) per annum, based on the average daily balance of said deposits to be credited quarterly.

Likewise, institutions may also maintain a special demand deposit account with local banks exclusively for trust duties.

Effective 1 July 2003, published interest rates that will be applied on BSP's Special Deposit Accounts of QBs shall be inclusive of the ten percent (10%) VAT.

b. The portion of reserves that may be maintained in the form of short-term market-yielding government securities refers to government securities shall be purchased directly from the BSP Treasury

[1] From 6% to 9% regular reserve effective the reserve week starting 7 January 2005 under MAB dated 29 December 2004 and from 9% to 10% regular reserve effective the reserve week starting 15 July 2005 under Circular 491 dated 12 July 2005
[2] From 10 % to 11% under Circular 491 dated 12 July 2005, effective the reserve week starting 15 July 2005.

Department at one-half percent (1/2%) below the prevailing market rate for an equivalent term and volume and subject to BSP's firm commitment to buy back at any time at prevailing market rates. Such reserves in the form of short-term market-yielding government securities shall be in addition to other forms of eligible reserves such as cash in vault or on deposit with the BSP.

All purchases of said government securities shall be under the RoSS system of the BTr. Transactions covering said securities shall be recorded in accordance with the guidelines in *Appendix Q-21*.

§ 4405Q.7 *Computation of reserve position.* An institution authorized to engage in trust and other fiduciary business shall calculate daily the required and available reserves on the value per books of its peso-denominated CTFs and such other managed peso funds, as well as on TOFA-Others, based on the seven-day week, starting Friday and ending Thursday including Saturdays, Sundays, holidays, non-business days and days when there is no clearing: *Provided,* That with reference to holidays, non-business days and days where there is no clearing, the reserve position at the close of business day immediately preceding such holidays, non-business days and days where there is no clearing, shall apply thereon. For the purpose of computing reserve position, the principal office in the Philippines and all branches and agencies located therein shall be treated as a single unit.

The required reserves in the current period (reference reserve week) shall be computed based on the corresponding levels of peso-denominated CTFs and such other managed peso funds, as well as TOFA-Others of the prior week.

For purposes of computing the required and available statutory and liquidity reserves for peso-denominated CTFs and such other managed peso funds, as well as TOFA-Others, the term *value per books* shall refer to the total volume of CTFs, other managed peso funds, as well as TOFA-Others less booked "Allowance for Probable Losses".

(As amended by Circular No. 535 dated 04 July 2006)

§ 4405Q.8 *Reserve deficiencies; sanctions.* The provisions of Section 4257Q shall govern the computation of reserve deficiencies for peso-denominated CTFs and such other managed peso funds, as well as for TOFA-Others, of institutions authorized to engage in trust and other fiduciary business, including the sanctions provided in said Subsection.

§ 4405Q.9 *Report of compliance* Every institution shall make a weekly report to the BSP of its daily required and available reserves on peso-denominated CTFs and such other managed peso funds, as well as on TOFA-Others, to be submitted not later than the close of the third business day following the reference week.

Sec. 4406Q Organization and Management

§ 4406Q.1 *Organization.* An institution authorized to engage in trust and other fiduciary business shall, pursuant to Subsec. 4404Q.1, include in its by-laws, provisions on the organization plan or structure of the department, office or unit which shall conduct such business. The by-laws shall also include provisions on the creation of a trust committee, the appointment of a trust officer and other subordinate officers and a clear definition of their duties and responsibilities as well as their line and staff functional relationships within the organization which shall be in accordance with the following guidelines:

a. Trust and other fiduciary business of an institution shall be carried out through a trust department which shall be

organizationally, operationally, administratively and functionally separate and distinct from the other departments and/or businesses of the institution.

An institution which is also engaged in investment management activities shall conduct the same only through its trust department and the responsibilities of the board of directors, trust committee and trust officer shall be construed to include the proper administration and management of investment management activities.

No institution shall undertake any of the trust and other fiduciary business and, whenever applicable, investment management activities outside the direct control, authority and management of the trust department or through any department or office which is involved in the other businesses of the institution, such as the Treasury, Funds Management or any similar department; otherwise, any such business shall be considered part of the institution's real liabilities.

The institution proper and the trust department may share the following activities: (1) electronic data processing; (2) credit investigation; (3) collateral appraisal; and (4) messengerial, janitorial and security services.

b. The trust department, trust officer and other subordinate officers of the trust department shall only be directly responsible to the institution's trust committee which shall, in turn, be only directly responsible to the institution's board of directors.

No director, officer or employee taking part in the management of trust and other fiduciary accounts shall perform duties in other departments or the audit committee of the institution and vice versa. However, branch managers duly authorized by the board of directors may, for or on behalf of the officer, sign predrawn trust instruments such as CTFs.

c. The organization structure and definition of duties and responsibilities of the trust committee, officers and employees of the trust department shall reflect adherence to the minimum internal control standards prescribed by the BSP.

d. Provisions shall be made by the institution to have legal assistance readily available in the review of proposed and/or existing trust and fiduciary agreements and documents and in the handling of legal and tax matters related thereto.

§ 4406Q.2 *Composition of trust committee.* The trust committee shall be composed of at least five (5) members including the president, the trust officer and directors who are appointed by the board of directors on a regular rotation basis and who are not officers of the institution proper. No member of the audit committee, if the institution has any, shall be concurrently designated as a member of the trust committee: *Provided,* That in the case of a trust committee composed of more than five (5) members, the appointment therein of an operating officer may be allowed only if the required balance in the membership of at least three (3) members of the board for every operating officer shall be maintained.

For purposes of this Subsection, the term *officer* shall include the president, executive vice-president, general manager, corporate secretary, treasurer and others mentioned as officers of the institution, or those whose duties as such are defined in the by-laws, or are generally known to be officers of the institution (or any of its branches and offices other than the Head Office) either through announcement, representation, publication or any kind of communication made by the institution.

The board of directors shall duly note in the minutes the committee members and

designate the chairman who shall be one of the directors referred to above.

§ 4406Q.3 ***Qualifications of committee members, officers and staff.*** The institution's trust department shall be staffed by persons of competence, integrity and honesty. Directors, committee members and officers charged with the administration of trust and other fiduciary activities shall, in addition to meeting the qualification standards prescribed for directors and officers of FIs, possess the necessary technical expertise in such business: *Provided,* That trust officers who shall be appointed shall have at least five (5) years of actual experience in trust operations, or at least three (3) years of actual experience in trust operations and completed at least one (1) year training program in trust operations acceptable to the BSP, or at least five (5) years of actual experience as officer of a bank, NBFI or related activities and completed at least one (1) year training program in trust operations acceptable to the BSP.

(As amended by Circular No. 665 dated 04 September 2009)

§ 4406Q.4 ***Responsibilities of administration***

a. *Board of Directors*. The board of directors is responsible for the proper administration and management of trust and other fiduciary business. Funds and properties held in trust or in any fiduciary capacity shall be administered with the skill, care, prudence and diligence necessary under the circumstances then prevailing that a prudent man, acting in like capacity and familiar with such matters, would exercise in the conduct of an enterprise of like character and with similar aims.

The responsibilities of the board of directors shall include, but need not be limited to the following:

(1) It shall determine and formulate general policies and guidelines on the: (a) acceptance, termination, or closure of trust and other fiduciary accounts; (b) proper administration and management of each trust and other fiduciary accounts; and (c) investment, reinvestment and disposition of funds or property held in its capacity as trustee or fiduciary;

(2) It shall direct and review the actions of the trust committee and all officers and employees designated to manage the trust and other fiduciary accounts, especially accounts without specific agreements on investments or discretionary accounts;

(3) It shall approve or confirm the acceptance, termination or closure of all trust and other fiduciary accounts and shall record such in its minutes;

(4) Upon the acceptance of an account, it shall immediately review all non-cash assets received for management. Likewise, it shall make a review of the trust and/or fiduciary assets at least once every twelve (12) months to determine the advisability of retaining or disposing of such assets;

(5) It shall be responsible for taking appropriate action on the examination reports of supervisory agencies, internal and/or external auditors on the institution's trust and other fiduciary business and recording such actions thereon in the minutes;

(6) It shall designate the members of the trust committee, the trust officer and subordinate officers of the trust department and shall be responsible for requiring reports from said committee and officers and recording its actions thereon in the minutes; and

(7) It shall establish an appropriate staffing pattern and adopt operating budgets that shall enable the trust department to effectively carry out its functions. It shall likewise be responsible for providing the officers and staff of the institution with appropriate training programs in the administration and operation of all phases of trust and other fiduciary business.

The board of directors may, by action duly entered in the minutes, delegate its authority for the acceptance, termination, closure or management of trust and other fiduciary accounts to the trust committee or to the trust officer, subject to certain guidelines approved by the board.

b. *Trust Committee*. The trust committee duly constituted and authorized by the board of directors shall act within the sphere of authority which may be provided in the by-laws and/or as may be delegated by the board, such as, but not limited to, the following:

(1) The acceptance and closing of trust and other fiduciary accounts;

(2) The initial review of assets placed under the trustee's or fiduciary's custody;

(3) The investment, reinvestment and disposition of funds or property;

(4) The review and approval of transactions between trust and/or fiduciary accounts; and

(5) The review of trust and other fiduciary accounts at least once every twelve (12) months to determine the advisability of retaining or disposing of the trust or fiduciary assets, and/or whether the account is being managed in accordance with the instrument creating the trust or other fiduciary relationship.

For this purpose, the trust committee shall meet whenever necessary and keep minutes of its actions and make periodic reports thereon to the board.

c. *Trust Officer*. The trust officer designated by the board of directors as head of the Trust Department shall act and represent the institution in all trust and other fiduciary matters within the sphere of his authority as may be provided in the by-laws or as may be delegated by the board. His responsibilities shall include, but need not be limited to, the following:

(1) The administration of trust and other fiduciary accounts;

(2) The implementation of policies and instructions of the board of directors and the trust committee;

(3) The submission of reports on matters which require the attention of the trust committee and the board of directors;

(4) The maintenance of adequate books, records and files for each trust or other fiduciary account; and

(5) The maintenance of necessary controls and measures to protect assets under his custody and held in trust or other fiduciary capacity.

§ 4406Q.5 - 4406Q.8 *(Reserved)*

§ 4406Q.9 *Outsourcing services in trust departments.* Trust departments of QBs performing trust and other fiduciary business and investment management activities are covered by the requirement of prior BSP approval for outsourcing services under *Appendix Q-37*.
(M-2007-009 dated 22 March 2007)

§ 4406Q.10 *Approval of the appointment/designation of trust officers.* Regardless of rank, the appointment/designation of trust officers shall require prior approval of the Monetary Board. The bio-data of the proposed trust officers shall be submitted to the appropriate department of the SES.

The appointment/designation of all incumbent trust officers not previously approved/confirmed by the Monetary Board shall be submitted, within six (6) months from 24 September 2009, to the BSP, through the appropriate department of the SES, for approval.
(Circular 665 dated 04 September 2009)

Sec. 4407Q Non-Trust, Non-Fiduciary and/or Non-Investment Management Activities The basic characteristic of trust, other fiduciary and investment management relationship is the absolute non-existence

of a debtor-creditor relationship, thus, there is no obligation on the part of the trustee, fiduciary or investment manager to guarantee returns on the funds or properties regardless of the results of the investment. The trustee, fiduciary or investment manager is entitled to fees/commissions which shall be stipulated and fixed in the contract or indenture and the trustor or principal is entitled to all the funds or properties and earnings less fees/commissions, losses and other charges. Any agreement/arrangement that does not conform to these shall not be considered as trust, other fiduciary or investment management relationship.

The following shall not constitute a trust, other fiduciary and/or investment management relationship:

a. When there is a preponderance of purpose or of intent that the arrangement creates or establishes a relationship other than a trust, fiduciary and/or investment management;

b. When the agreement or contract is itself used as a certificate of indebtedness in exchange for money placement from clients and/or as the medium for confirming placements and investment thereof;

c. When the agreement or contract of an account is accepted under the signature(s) of those other than the trust officer or subordinate officer of the trust department or those authorized by the board of directors to represent the trust officer;

d. Where there is a fixed rate or guaranty of interest, income or return in favor of its client or beneficiary: *Provided, however,* That where funds are placed in fixed income-generating investments, a quotation of *income expectation* or like terms, shall neither be considered as arrangements with a fixed rate nor a guaranty of interest, income or return when the agreement or indenture categorically states in bold letters that the quoted income expectation or like terms is neither assured nor guaranteed by the trustee or fiduciary and it does not, therefore, entitle the client to a fixed interest or return on his investments: *Provided, further,* That any of the following practices or practices similar and/or tantamount thereto shall be construed as fixing or guaranteeing the rate of interest, income or return:

(1) Issuance of certificates, side agreements, letters of undertaking, or other similar documents providing for fixed rates or guaranteeing interest, income or return;

(2) Paying trust earnings based on indicated or expected yield regardless of the actual investment results;

(3) Increasing or reducing fees in order to meet a quoted or expected yield; and

(4) Entering into any arrangement, scheme or practice which results in the payment of fixed rates or yield on trust investments or in the payment of the indicated or expected yield regardless of the actual investment results; and

e. Where the risk or responsibility is exclusively with the trustee, fiduciary or investment manager in case of loss in the investment of trust, fiduciary or investment management funds, when such loss is not due to the failure of the trustee or fiduciary to exercise the skill, care, prudence and diligence required by law.

Trust, other fiduciary and investment management activities involving any of the foregoing which are accepted, renewed or extended after 16 October 1990 shall be reported as deposit substitutes and shall be subject to the reserve requirement for deposit substitutes from the time of inception, without prejudice to the imposition of the applicable sanctions provided for in Sections 36 and 37 of R.A. No. 7653, and Sections 12 and 16 of P.D. No. 129, as amended.

Sec. 4408Q Unsafe and Unsound Practices. Whether a particular activity may be considered as conducting business in an unsafe or unsound manner, all relevant facts

must be considered. An analysis of the impact thereof on the QB's/trust entity's operations and financial conditions must be undertaken, including evaluation of capital position, asset condition, management, earnings posture and liquidity position.

In determining whether a particular act or omission, which is not otherwise prohibited by any law, rule or regulation affecting QBs/trust entities, may be deemed as conducting business in an unsafe or unsound manner, the Monetary Board, upon report of the head of the SES based on findings in an examination or a complaint, shall consider any of the following circumstances:

a. The act or omission has resulted or may result in material loss or damage, or abnormal risk or danger to the safety, stability, liquidity or solvency of the institution;

b. The act or omission has resulted or may result in material loss or damage or abnormal risk to the institution's depositors, creditors, investors, stockholders, or to the BSP, or to the public in general;

c. The act or omission has caused any undue injury, or has given unwarranted benefits, advantage or preference to the QB/ trust entity or any party in the discharge by the director or officer of his duties and responsibilities through manifest partiality, evident bad faith or gross inexcusable negligence; or

d. The act or omission involves entering into any contract or transaction manifestly and grossly disadvantageous to the QB/trust entity, whether or not the director or officer profited or will profit thereby.

The list of activities which may be considered unsafe and unsound is shown in *Appendix Q-24*.

In line with the statement of principles governing trust and other fiduciary business under Sec. 4401Q, the trustee, fiduciary or investment manager shall desist from the following unsound practices:

a. Entering in an arrangement whereby the client is at the same time the borrower of his own fund placement, or whereby the trustor or principal is a borrower of other trust, fiduciary or investment management funds belonging to the same family or business group of such trustor or principal;

b. Granting loans or accommodations to any trust committee member, officer and employee of the trust department except where such loans are obtained by said persons as members of an employee benefit fund of the trustee's own institution;

c. Borrowing from, or selling trust, other fiduciary and/or investment management assets to, the trust corporation or IH proper to cover portfolio losses and/or to guarantee the return of principal or income;

d. Granting new loans to any borrower who has a past due and/or classified loan account with the institution itself or its trust department; and

e. Requiring clients to sign documents in blank.

(As amended by Circular No. 640 dated 16 January 2009)

§§ 4408Q.1 - 4408Q.8 *(Reserved)*

§ 4408Q.9 *Sanctions*. The Monetary Board may, at its discretion and based on the seriousness and materiality of the acts or omissions, impose any or all of the following sanctions provided under Section 37 of R.A. No. 7653 and Section 56 of R.A. No. 8791, whenever a QB/trust entity conducts business in an unsafe and unsound manner:

a. Issue an order requiring the QB/trust entity to cease and desist from conducting business in an unsafe and unsound manner and may further order that immediate action be taken to correct the conditions resulting from such unsafe or unsound practice;

b. Fines in amounts as may be determined by the Monetary Board to be appropriate, but in no case to exceed

P30,000 a day on a per transaction basis taking into consideration the attendant circumstances, such as the gravity of the act or omission and the size of the QB/trust entity, to be imposed on the QB/trust entity, their directors and/or responsible officers;

c. Suspension of lending or foreign exchange operations or authority to accept new deposit substitutes and/or new trust accounts or to make new investments;

d. Suspension of responsible directors and/or officers;

e. Revocation of quasi-banking license and/or trust authority; and/or

f. Receivership and liquidation under Section 30 of R.A. No. 7653.

All other provisions of Sections 30 and 37 of R.A. No. 7653, whenever appropriate, shall also be applicable on the conduct of business in an unsafe or unsound manner.

The imposition of the above sanctions is without prejudice to the filing of appropriate criminal charges against culpable persons as provided in Sections 34, 35 and 36 of R.A. No. 7653.

(Next page is Part IV- Page 15)

Sec. 4409Q Trust and Other Fiduciary Business. The conduct of trust and other fiduciary business shall be subject to the following regulations.

§ 4409Q.1 ***Minimum documentary requirements.*** Each trust or fiduciary account shall be covered by a written document establishing such account, as follows:

a. In the case of accounts created by an order of the court or other competent authority, the written order of said court or authority.

b. In the case of accounts created by corporations, business firms, organizations or institutions, the voluntary written agreement or indenture entered into by the parties, accompanied by a copy of the board resolution or other evidence authorizing the establishment of, and designating the signatories to, the trust or other fiduciary account.

c. In the case of accounts created by individuals, the voluntary written agreement or indenture entered into by the parties.

The voluntary written agreement or indenture shall include the following minimum provisions:

(1) Title or nature of contractual agreement in noticeable print;

(2) Legal capacities, in noticeable print, of parties sought to be covered;

(3) Purposes and objectives;

(4) Funds and/or properties subject of the arrangement;

(5) Distribution of the funds and/or properties;

(6) Duties and powers of trustee or fiduciary;

(7) Liabilities of the trustee or fiduciary;

(8) Reports to the client;

(9) Termination of contractual arrangement and, in appropriate cases, provision for successor-trustee or fiduciary;

(10) The amount or rate of the compensation of trustee or fiduciary;

(11) A statement in noticeable print to the effect that trust and other fiduciary business are not covered by the PDIC and that losses, if any, shall be for the account of the client; and

(12) Disclosure requirements for transactions requiring prior authority and/or specific written investment directive from the client, court of competent jurisdiction or other competent authority.

§ 4409Q.2 ***Lending and investment disposition.*** Assets received in trust or in other fiduciary capacity shall be administered in accordance with the terms of the instrument creating the trust or other fiduciary relationship.

When a trustee or fiduciary is granted discretionary powers in the investment disposition of trust or other fiduciary funds and unless otherwise specifically enumerated in the agreement or indenture and directed in writing by the client, court of competent jurisdiction or other competent authority, loans and investments of the fund shall be limited to:

a. Evidences of indebtedness of the Republic of the Philippines and of the BSP, and any other evidences of indebtedness or obligations the servicing and repayment of which are fully guaranteed by the Republic of the Philippines or loans against such government securities;

b. Loans fully guaranteed by the Republic of the Philippines as to the payment of principal and interest;

c. Loans fully secured by a hold-out on, assignment or pledge of deposit substitutes of the institution or deposits with other banks, or mortgage and chattel mortgage bonds issued by the trustee or fiduciary;

d. Loans fully secured by real estate or chattels in accordance with Section 78 of R.A. No. 337, as amended, and subject to the requirements of Sections 75, 76 and 77 of R.A. No. 337, as amended; and

e. Investment in the BSP special deposit account (SDA) facility made in accordance with the guidelines in *Appendix Q-46*.

The specific directives required under this Subsection shall consist of the following information:

(1) The transaction to be entered into;
(2) The borrower's name;
(3) Amount involved; and
(4) Collateral security(ies), if any.

(As amended by M-2007-038 dated 29 November 2007 and M-2007-011 dated 08 May 2007)

§ 4409Q.3 *Transactions requiring prior authority.* A trustee or fiduciary shall not undertake any of the following transactions for the account of a client, unless prior to its execution, such transaction has been fully disclosed and specifically authorized in writing by the client, beneficiary, other party-in-interest, court of competent jurisdiction or other competent authority:

a. Lend, sell, transfer or assign money or property to any of the departments, directors, officers, stockholders or employees of the trustee or fiduciary, or relatives within the first degree of consanguinity or affinity, or the related interests of such directors, officers and stockholders; or to any corporation where the trustee or fiduciary owns at least fifty percent (50%) of the subscribed capital or voting stock in its own right and not as trustee nor in a representative capacity;

b. Purchase or acquire property or debt instruments from any of the departments, directors, officers, stockholders, or employees of the trustee or fiduciary, or relatives within the first degree of consanguinity or affinity, or the related interest of such directors, officers and stockholders; or from any corporation where the trustee or fiduciary owns at least fifty percent (50%) of the subscribed capital or voting stock in its own right and not as trustee nor in a representative capacity;

c. Invest in equities of, or in securities underwritten by, the trustee or fiduciary or a corporation in which the trustee or fiduciary owns at least fifty percent (50%) of the subscribed capital or voting stock in its own right and not as trustee nor in a representative capacity; and

d. Sell, transfer, assign, or lend money or property from one trust or fiduciary account to another trust or fiduciary account except where the investment is in any of those enumerated in Items *"a"* to *"d"* of Subsec. 4409Q.2.

Directors, officers, stockholders, and their related interest covered by this Subsection shall be those considered as such under existing regulations on loans to DOSRI in Part III-E of this Manual. The procedural and reportorial requirements in said regulations shall also apply.

The disclosure required under this Subsection shall consist of the following minimum information:

(1) The transactions to be entered into;
(2) Identities of the parties involved in the transactions and their relationships (shall not apply to Item *"d"* of this Subsection);
(3) Amount involved; and
(4) Collateral security(ies), if any.

The above information shall be made known to clients in a separate instrument or in the very instrument creating the trust or fiduciary relationship.

§ 4409Q.4 *Ceilings on loans.* Loans funded by trust accounts shall be subject to the single borrower's loan limit and DOSRI ceilings imposed on QBs under Part III - A and - E of this Manual. For purposes of determining compliance with said ceilings, the total amount of said loans granted by the institution and its trust department to the same person, firm or corporation shall be combined.

§ 4409Q.5 ***Funds awaiting investment or distribution.*** Funds held by the trustee or fiduciary awaiting investment or distribution shall not be held uninvested or undistributed any longer than is reasonable for the proper management of the account.

§ 4409Q.6 ***Other applicable regulations on loans and investments - trust and other fiduciary accounts.*** The loans and investments of trust and other fiduciary accounts shall be subject to pertinent laws, rules and regulations for QBs that shall include, but need not be limited to, the following:

a. Requirements of Sections 39 and 40 of R.A. No. 8791 (The General Banking Law of 2000);

b. Provisions of Section 4(e) of the New Rules on Registration of Short-Term Commercial Papers and Section 7(f) of the New Rules on the Registration of Long-Term Commercial Papers issued by the SEC (*Appendices Q-7* and *Q-8*).

c. Criteria for past due accounts; and

d. Qualitative appraisal of loans, investments and other assets that may require provisions for probable losses which shall be booked in accordance with the Financial Reporting Package for Trust Institutions (FRPTI);

e. Requirements of Sections 3 and 8 of the Securities and Regulation Code (SRC); and

f. Provisions of Section 44 – Investments by Philippine residents – of the BSP Manual of Regulations on Foreign Exchange Transactions (FX Manual), such that the cross-currency investments of peso trust and other fiduciary accounts, including peso unit investment trust (UIT) funds, shall be subject to the following conditions:

(1) All cash flows of the trustee or fiduciary shall only be in pesos. In case the foreign exchange acquired or received by the trustee or fiduciary as dividends/ earnings or divestment proceeds on such investment are intended for reinvestment abroad, the same proceeds are not required to be inwardly remitted and sold for pesos through authorized agent banks: *Provided,* That such proceeds are reinvested abroad within two (2) banking days from receipt of the funds abroad;

(2) The trustee or fiduciary shall purchase, invest, reinvest, sell, transfer or dispose foreign currency-denominated financial instruments, including securities as defined in Section 3 of the SRC, through a distributor or underwriter duly authorized or licensed by the government of the issuer of such instruments, or a counterparty FI (seller or buyer) accredited by the trustee or fiduciary: *Provided,* That, the conduct, documentation, and settlement of any of these transactions shall be outside Philippine jurisdiction;

(3) The trustee of fiduciary shall record cross-currency investment transactions in the peso regular books at their foreign currency amounts and their local currency equivalent using the Philippine Dealing System peso/US dollar closing rate and the New York US dollar/third currencies closing rate; and

(4) The trustee or fiduciary shall comply with the reportorial requirements that may be prescribed by the BSP, which shall include as a minimum, the foreign currency amount and the local currency equivalent of the total cross currency investments with details on: (a) type of investments; and (b) amount of cash flow converted.

For purposes of this Subsection, "*resident*", as defined under Section 1 of the FX Manual, shall refer to the (a) trustee or fiduciary that administers the assets received in trust or in other fiduciary capacity; or (b) principal that engages the services of the investment manager under an investment management agreement.

(As amended by Circular No. 676 dated 29 December 2009)

§ 4409Q.7 *Operating and accounting methodology*. Trust and other fiduciary accounts shall be operated and accounted for in accordance with the following:

a. The trustee or fiduciary shall administer, hold or manage the fund or property in accordance with the instrument creating the trust or other fiduciary relationship; and

b. Funds or property of each client shall be accounted separately and distinctly from those of other clients herein referred to as *individual account accounting*.

§ 4409Q.8 *Tax-exempt individual trust accounts.* The following shall be the features/ requirements of individual trust accounts which may be exempted from the twenty percent (20%) final tax under Section 24(B)(1) of R.A. No. 8424 (The Tax Reform Act of 1997):

a. The tax exemption shall apply to trust indentures/agreements contracted on or after 03 January 2000;

b. The trust indenture/agreement shall only be between individuals who are Filipino citizens or resident aliens and QBs acting as trustee. The trust indenture/agreement shall be non-negotiable and non-transferable;

c. The trust indenture/agreement shall indicate that pursuant to Section 24(B)(1) of R.A. No. 8424, interest income of the trust fund derived from investments in interest-bearing instruments (e.g., time deposits, government securities, loans and other debt instruments) which are otherwise subject to the twenty percent (20%) final tax shall be exempt from said final tax provided the fund was held by the trustee-QB for at least five (5) years. If said fund was held for a period less than five (5) years interest income shall be subject to a final tax based on the following schedule –

Holding Period	Rate of Tax
Four (4) years to less than five (5) years	5%
Three (3) years to less than four (4) years	12%
Less than three (3) years	20%

Necessarily, the trust indenture/ agreement shall clearly indicate the date when the trustee-bank actually received the trust funds which shall serve as basis for determining the holding period of the funds.

d. A trustee may accept additional funds for inclusion in trust accounts which have been established as tax-exempt under R.A. No. 8424. However, the receipt of additional funds shall be properly documented by indicating that they are part of existing tax-exempt trust accounts and that the interest income of the additional funds derived from investments in interest-bearing instruments shall be exempt from the twenty percent (20%) final tax under the same conditions mentioned in the preceding item. The document shall also indicate the date when the funds were received by the trustee-bank to serve as basis for determining the minimum five (5) - year holding period for tax exemption purposes of the additional funds; and

e. Tax-exempt individual trust accounts established under this Subsec. shall be subject to the provisions of Subsecs. 4409Q.1(c) and 4409Q.2 up to 4409Q.7.

§ 4409Q.9 *Living trust accounts* The guidelines on living trust accounts are as follows:

a. *Definition*. *Living Trust* is defined under the Manual of Accounts for Trust, as a personal trust created by agreement. It becomes operational during the lifetime of the trustor as soon as the agreement is accomplished.

Under a living trust, the trustor (also known as settlor) conveys property or a sum of money to be managed by the trustee, as the agreement dictates, for the benefit of the trustor and third person(s) or third person(s) only. However, the trustor/s cannot create a trust with himself/ themselves as the sole beneficiary/(ies). The functions and authorities of the trustee as defined in the agreement shall include:

(1) the purpose or intention of the trust;

(2) the nature and value of the property or sum of money that comprise the trust;

(3) the trustee's investment powers;

(4) the name(s) of the beneficiaries; and

(5) the terms and conditions under which the income and/or principal of the trust is to be paid or to be disposed of during the lifetime and ultimately, upon the death of the trustor or upon the occurrence of a specified event(s).

A living trust may either be revocable or irrevocable.

b. *Minimum criteria*. In line with such definition, transactions considered as living trust accounts should meet the following minimum criteria:

(1) Minimum entry amount and maintaining balance shall at least be P100,000: *Provided*, That living trust accounts with balances of up to P500,000 shall only be invested in deposits and government securities;

(2) Living trust accounts shall be maintained for a minimum period of six (6) months. The termination of the living trust agreement, for any cause, within the minimum holding period shall render the trustor ineligible from opening a new living trust account within a period of one (1) year from termination date;

(3) Reversion of any part of the principal to the trustor, except in cases provided under the dispositive portion, shall be allowed only upon termination of the living trust agreement: *Provided,* That in no case can there be a complete or substantial reversion of the principal pursuant to the dispositive portion within the minimum holding period nor can the principal fall below P100,000;

(4) Any living trust account that does not meet the requirement on the minimum entry and minimum maintaining balance or is not invested in qualified outlets shall be considered as other fiduciary accounts subject to applicable reserve and other requirements;

(5) Pre-printed living trust agreements may be allowed for expediency: *Provided* That the sections for the trust purpose and the dispositive provision are left blank and shall only be filled-up upon the client's signing thereof. The purpose shall categorically state the real intention of the trustor, which may include, but need not be limited to:

(a) providing his/her and beneficiary/(ies) present and/or future financial support;

(b) protecting his/her beneficiary/(ies) against his/her inexperience in business matters;

(c) preventing him/her from making imprudent expenditures;

(d) prevent the beneficiary/(ies) from living beyond their means in case of outright disposition of assets in their favor;

(e) protecting the beneficiary/(ies) against unforeseen contingencies such as incompetency, incapacity, physical disability or similar misfortune; and

(f) setting aside and segregating particular assets, proceeds or payments for administration and distribution pursuant to a court decree or by agreement.

The dispositive provision should clearly and specifically define the terms and conditions under which the principal and/or income shall be distributed in order to accomplish such purpose/(s), by taking into consideration the frequency of redemption; the respective interests of each beneficiary; and to whom the proceeds shall be payable. Redemption of funds shall strictly be in accordance with the said terms and conditions; and

(6) A living trust account may be opened jointly under one (1) living trust agreement by related individuals up to the second degree of consanguinity or affinity: *Provided,* That the requirements under Item *"5"* above are fully complied with. Unrelated individuals or those beyond the second degree of consanguinity or affinity may likewise open a joint living trust account

§ 4409Q.9
09.12.31

under one (1) living trust agreement: *Provided*, That the minimum contribution of each individual is at least P100,000: *Provided further*, That the trust is for a common purpose and: *Provided, finally*, That the requirements under Item *"5"* are fully complied with.

c. *Marketing.* Officers and personnel of the institution proper, including branch managers, shall not be allowed to market living trust products and sign pre-printed living trust agreements. However, branch managers/officers may be allowed to refer clients to the Trust Department and give short introduction on the living trust products to prospective clients.

d. *Transitory Provision.* Outstanding living trust accounts that do not meet the foregoing additional requirements shall be given twelve (12)[1] months from 11 April 2006 to comply with the aforestated requirements; otherwise, such accounts shall be considered as Other Fiduciary Accounts subject to applicable reserve requirements.

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[1] Original 6 months transitory period under Circular No. 521 extended by another 6 months under Circular No. 553.

e. *Sanctions*. Any violation of the provisions of this Subsection shall be subject to the sanctions provided under Section 37 of R.A. No. 7653 (The New Central Bank Act).

(Circular Nos. 553 dated 22 December 2006 and 521 dated 21 March 2006)

§§ 4409Q.10 - 4409Q.15 *(Reserved)*

§ 4409Q.16 *Qualification and accreditation of quasi-banks acting as trustee on any mortgage or bond issuance by any municipality, government-owned or controlled corporation, or any body politic*

a. *Applicability*. QBs duly accredited by the BSP may act as trustee on any mortgage or bond issued by any municipality, GOCC, or any body politic.

b. *Application for accreditation*. A QB desiring to act as trustee on any mortgage or bond issued by any municipality, GOCC, or any body politic shall file an application for accreditation with the appropriate department of the SES. The application shall be signed by the president or officer of equivalent rank of the QB and shall be accompanied by the following documents:

(1) certified true copy of the resolution of the institution's board of directors authorizing the application;

(2) a certification signed by the president or officer of equivalent rank that the institution has complied with all the qualification requirements for accreditation.

c. *Qualification requirements*. A QB applying for accreditation to act as trustee on any mortgage or bond issued by any municipality, GOCC, or any body politic must comply with the requirements in *Appendix Q-31*.

d. *Independence of the trustee*. A QB is prohibited from acting as trustee of a mortgage or bond issuance if any elective or appointive official of the LGU, GOCC, or body politic which issued said mortgage or bond and/or his related interests own such number of shares of the QB that will allow him or his related interests to elect at least one (1) member of the board of directors of such QB or is directly or indirectly the registered or beneficial owner of more than ten percent (10%) of any class of its equity security.

e. *Investment and management of the funds*. A domestic QB designated as trustee of a mortgage or bond issuance may hold and manage, in accordance with the provisions of the trust indenture or agreement, the proceeds of the mortgage or bond issuance and such assets and funds of the issuing municipality, corporation, or body politic as may be required to be delivered to the trustee under the Trust indenture/agreement, subject to the following conditions/restrictions:

(1) Pending the utilization of such funds pursuant to the provisions of the trust indenture/agreement, the same shall only be (i) deposited in a bank authorized to accept deposits from the Government or government entities: *Provided,* That the depository bank is not a subsidiary or affiliate of the trustee QB, or (ii) invested in peso-denominated treasury bills acquired/purchased from any securities dealer/entity, other than the trustee or any of its unit/department, its subsidiary or affiliate.

(2) Investments of funds constituting or forming part of the sinking fund created as the primary source for the payment of the principal and interests due the mortgage or bonds shall also be limited to deposits in any bank authorized to accept deposits from the Government or government entities and investments in government securities that are consistent with such purpose which must be acquired/purchased from any securities dealer/entity, other than the trustee or any of its unit/department, its subsidiary or affiliate.

f. *Waiver of confidentiality*. A QB designated as trustee of any mortgage or bond issued by any municipality, GOCC, or any body politic shall submit to the appropriate department of the SES a waiver of the confidentiality of information under Sections 2 and 3 of R.A. No. 1405, as amended, duly executed by the issuer of the mortgage or bond in favor of the BSP.

g. *Reportorial requirements*. A QB authorized by the BSP to act as trustee of the proceeds of mortgage or bond issuance of a municipality, GOCC, or body politic shall comply with reportorial requirements that may be prescribed by the BSP.

h. *Applicability of the rules and regulations on Trust, Other Fiduciary Business and Investment Management Activities*. The provisions of the Rules and Regulations on Trust, Other Fiduciary Business and Investment Management Activities not inconsistent with the provisions of this Subsection shall form part of these rules.

i. *Sanctions*. Without prejudice to the penal and administrative sanctions provided for under Sections 36 and 37, respectively, of the R.A. No. 7653, violation of any provision of this Subsection shall be subject to the following sanctions/ penalties depending on the gravity of the offense:

(1) *First offense* –

(a) Fine of up to P10,000 a day for the institution for each violation reckoned from the date the violation was committed up to the date it was corrected; and

(b) Reprimand for the directors/officers responsible for the violation.

(2) *Second offense* –

(a) Fine of up to P20,000 a day for the institution for each violation reckoned from the date the violation was committed up to the date it was corrected;

(b) Suspension for ninety (90) days without pay for directors/officers responsible for the violation; and

(c) Revocation of the authority to act as trustees on any mortgage or bond issuance by any municipality, GOCCs, or body politic.

(3) *Subsequent offense* –

(a) Fine of up to P30,000 a day for the institution for each violation reckoned from the date the violation was committed up to the date it was corrected;

(b) Suspension or revocation of the trust license;

(c) Suspension for 120 days without pay of the directors/officers responsible for the violation.

§ 4409Q.17 *Trust fund of pre-need companies*. The following rules and regulations shall govern the acceptance, management and administration of the trust funds of pre-need companies by entities authorized to perform trust and other fiduciary functions.

a. *Administration of trust fund*. In line with the policy of providing greater protection to pre-need planholders, prudential measures are hereby laid out in the administration of trust funds of pre-need companies. The trust fund, inclusive of earnings, shall be administered and managed by the trustee with the skill, care, prudence and diligence necessary under the circumstances then prevailing that a prudent man, acting in the same capacity and familiar with such matters, would exercise in the conduct of an enterprise of a like character and similar aims.

The trustee shall have exclusive management and control over the trust fund and the right at any time to sell, convert, invest, change, transfer or otherwise dispose of the assets comprising the funds.

b. *Trustee*. No trust entity shall act as a trustee or administer or hold a trust fund established by a pre-need company, which is a subsidiary or affiliate, as defined under existing BSP regulations, of such trust entity.

Trust entities currently holding or administering trust funds of an affiliate pre-need company may continue to act as trustee of such funds after the transition period provided under Item *"g"* only upon prior approval of the Monetary Board on the basis of a clear showing that no potential conflict of interest will arise. An absence of any exception or finding on conflicts of interest during an examination of the trust entity shall be deemed as *prima facie* evidence that no potential conflict of interest will arise.

c. *Investment of the trust fund.* Unless otherwise allowed under existing laws or regulations issued by the agency having jurisdiction and supervision over pre-need companies, or with prior written approval by said agency, loans and investments of the trust funds shall be limited to:

(1) Evidences of indebtedness of the Republic of the Philippines and of the BSP, and any other evidences of indebtedness or obligations wherein the servicing and repayment of which are fully guaranteed by the Republic of the Philippines or loans against such government securities;

(2) Commercial papers duly registered with the SEC with a credit rating of one (1) for short term and "AAA" for long-term or their equivalent;

(3) Loans fully guaranteed by the Republic of the Philippines, as to the payment of principal and interest;

(4) Loans fully secured by a hold-out on, assignment or pledge of deposits maintained with banks, and/or of deposit substitutes or of mortgage and chattel mortgage bonds issued by the trustee/ fiduciary or by banks;

(5) Loans fully secured by real estate in accordance with Section 37 and subject to the requirements of Sections 39 and 40 of R.A. No. 8791 and their implementing regulations; and

(6) Loans fully secured by unconditional payment guarantees (such as standby letters of credit and letter of indemnity) issued by banks/multilateral FIs.

d. *Transactions with DOSRI.* The trustee shall not, for the account of the trustor or the beneficiary of the trust, purchase or acquire property from, or sell, transfer, assign or lend money or property to, or purchase debt instruments of, any of the departments, directors, officers, stockholders, employees, subsidiaries and affiliates of the trustee and/or the trustor, and relatives within the first degree of consanguinity or affinity, or the related interests, of such directors, officers and stockholders, without prejudice to any rule that may be issued by the agency having jurisdiction and supervision over such pre-need company allowing such transaction with the prior written approval of such agency. Such written approval shall clearly specify the amount of the loan and/or investment including the name of the concerned director, officer, stockholder and their related interests.

e. *Applicability of the Rules and Regulations on Trust, Other Fiduciary Business and Investment Management Activities (Trust Rules).* The provisions of the Trust Rules consistent with the provisions of this Subsection shall supplementarily apply to trust funds of pre-need companies.

f. *Penalties and sanctions.* Any violation of the provisions of this Subsection shall be a ground for prohibiting the concerned entity from accepting, managing and administering trust funds of pre-need companies without prejudice to the imposition of the applicable sanctions prescribed or allowed under the Trust Rules.

g. *Transitory provisions.* Institutions performing trust and other fiduciary business which are presently administering

and managing trust funds of pre-need companies are hereby given a period of one (1) year from 25 April 2006 to comply with the requirements hereof.

(Memorandum to All Banks and NBFIs dated 28 March 2006)

Sec. 4410Q Unit Investment Trust Funds/ Common Trust Funds[1]. The following rules and regulations shall govern the creation, administration and investment/s of Unit Investment Trust (UIT) Funds.

The rules and regulations on Common Trust Funds (CTFs) are in *Appendix Q-32*.

§ 4410Q.1 *Definition*

a. *Unit Investment Trust Funds*. Unit Investment Trust Funds are open-ended pooled trust funds denominated in pesos or any acceptable currency, which are operated and administered by a trust entity and made available by participation. The term Unit Investment Trust Fund is synonymous to CTFs. As an open-ended fund, participation or redemption is allowed as often as stated in its plan rules.

UIT Funds shall not include long term funds designed for the primary purpose of availing the tax incentives/exemption under Section 24(B)(1) of R.A. No. 8424 (The Tax Reform Act of 1997).

b. *Trust entity*. Any bank, IH or a stock corporation duly authorized by the Monetary Board to engage in trust, investment management and fiduciary business.

c. *Board of directors*. For this purpose, the term shall include a trust entity's duly constituted board of directors or its functional oversight equivalent which shall include the country head in the case of foreign institutions.

§ 4410Q.2 *Establishment of a Unit Investment Trust Fund.* Any trust entity authorized to perform trust functions may establish, administer and maintain one (1) or more UIT Funds subject to applicable provisions under this Section.

§ 4410Q.3 *Administration of a Unit Investment Trust Fund.* The trustee shall have exclusive management and control of each UIT Fund under its administration, and the sole right at any time to sell, convert, reinvest, exchange, transfer or otherwise change or dispose of the assets comprising the fund: *Provided,* That no participant in a UIT Fund shall have or be deemed to have any ownership or interest in any particular account or investment in the UIT Fund but shall have only its proportionate beneficial interest in the fund as a whole.

§ 4410Q.4 *Relationship of trustee with Unit Investment Trust Fund.* A trustee administering a UIT Fund shall not have any other relationship with such fund other than its capacity as trustee of the UIT Fund: *Provided, however,* That a trustee which simultaneously administers other trust, fiduciary or investment management funds may invest such funds in the trustee's UIT Fund, if allowed under a policy approved by the board of directors.

§ 4410Q.5 *Operating and accounting methodology.* A UIT Fund shall be operated and accounted for in accordance with the following:

a. The total assets and accountabilities of each fund shall be accounted for as a single account referred to as pooled-fund accounting method.

b. Contributions to each fund by clients shall always be through participation in units of the fund and each unit shall have uniform rights or privileges, as any other unit.

c. All such participations shall be pooled and invested as one (1) account (referred to as collective investments).

d. The beneficial interest of each participation unit shall be determined under a unitized net asset value per unit (NAVPu) valuation methodology defined in the written plan of the UIT Fund, and no

[1] The regulations on common trust funds (CTFs) were relocated to *Appendix Q-32*. UIT Funds regulations took effect on 01 October 2004 (effectivity of Circular 447 dated 03 September 2004).

participation shall be admitted to, or redeemed from, the fund except on the basis of such valuation. To arrive at a fund's NAVPu, the fund's total Net Assets is divided by the total outstanding units. *Total Net Assets* is a summation of the market value of each investment less fees, taxes, and other qualified expenses, as defined under the plan rules.

§ 4410Q.6 *Plan rules.* Each UIT Fund shall be established, administered and maintained in accordance with a written trust agreement drawn by the trustee, referred to as the "*Plan*" which shall be approved by the board of directors of the trustee and a copy of which shall be submitted to the BSP for processing and approval prior to its implementation. Each new UIT Fund Plan filed for approval shall be charged a processing fee of P10,000.00.

The Plan shall contain the following minimum elements:

a. *Title of the Plan*. This shall correspond to the product/brand name by which the UIT Fund is proposed to be known and made available to its clients. The Plan rules shall state the classification of the UIT Fund (e. g., money market fund, bond fund, balanced fund and equity fund).

b. *Manner by which the fund is to be operated*. A statement of the fund's investment objectives and policies including limitations, if any.

c. *Risk disclosure*. The Plan rules shall state both the general risks and risks specific to the type of fund.

d. *Investment powers of the trustee with respect to the fund, including the character and kind of investments, which may be purchased, by the fund*. There must be an unequivocal statement of the full discretionary powers of the trustee as far as the fund's investments are concerned. These powers shall be limited only by the duly stated investment objective and policies of the fund.

e. The unitized NAVPu valuation methodology as prescribed under Subsec. 4410Q.5.d shall be employed.

f. *Terms and conditions governing the admission or redemption of units of participation in the fund*. The Plan rules shall state that the trustee, prior to admission of a client's initial participation in the UIT Fund, shall conduct a client suitability assessment to profile the risk-return orientation and suitability of the client to the specific type of fund. If the frequency of admission or redemption is other than daily; that is, any business day, the same should be explicitly stated in the Plan rules: *Provided,* That the admission and redemption shall be based on the end of day NAVPu of the fund computed after the cut-off time for fund participation and redemption for that reference day, in accordance with existing BSP regulations on mark to market valuation of investment securities.

g. *Aside from the regular audit requirement applicable to all trust accounts, an external audit of each UIT Fund shall be conducted annually by an independent auditor acceptable to the BSP and the results thereof made available to participants*. The external audit shall be conducted by the same external auditor engaged for the audit of the trust entity.

h. *Basis upon which the fund may be terminated*. The Plan rules shall state the rights of participants in case of termination of the fund. Termination of the fund shall be duly approved by the trustee's board of directors and a copy of the resolution submitted to the appropriate department of the BSP.

i. *Liability clause of the trustee*. There must be a clear and prominent statement adjacent to where a client is required to sign the participating trust agreement that (1) the UIT Fund is a trust product and not a deposit account or an obligation of, or guaranteed, or insured by the trust entity or its affiliates or subsidiaries; (2) the UIT

Fund is not insured or governed by the PDIC; (3) due to the nature of the investment, yields and potential yields cannot be guaranteed; (4) any loss/income arising from market fluctuations and price volatility of the securities held by the UIT Fund, even if invested in government securities, is for the account of the client/ participant; (5) as such, the units of participation of the investor in the UIT Fund, when redeemed, may be worth more or be worth less than his/her initial investment contributions; (6) historical performance, when presented, is purely for reference purposes and is not a guarantee of similar future result; and (7) the trustee is not liable for losses unless upon willful default, bad faith or gross negligence.

j. *Amount of fees/commission and other charges to be deducted from the fund* The amount of fees that shall be charged to a fund shall cover the fund's fair and equitable share of the routine administrative expenses of the trustee such as salaries and wages, stationery and supplies, credit investigation, collateral appraisal, security, messengerial and janitorial services, EDP expenses, BSP supervision fees and internal audit fees. However, the trustee may charge a UIT Fund for special expenses in case such expenses are (1) necessary to preserve or enhance the value of the fund, (2) payable to a third party covered by a separate contract, and (3) disclosed to participants. The trustee shall secure prior BSP approval for outsourcing services provided under existing regulations. No other fees shall be charged to the fund.

Marketing or other promotional related expenses shall be for the account of the trustee and shall be presumed covered by the trust fee.

k. Such other matters as may be necessary or proper to define clearly the rights of participants in the UIT Fund. The provisions of the Plan shall govern participation in the fund including the rights and benefits of persons having interest in such participation, as beneficiaries or otherwise. The Plan may be amended by a resolution of the board of directors of the trustee: *Provided, however,* That participants in the fund shall be immediately notified of such amendments and shall be allowed to withdraw their participations within a reasonable time but in no case less than thirty (30) calendar days after the amendments are approved, if they are not in conformity with the amendments made thereto: *Provided further,* That amendments to the Plan shall be submitted to the BSP within ten (10) business days from approval of the amendments by the board of directors. For purposes of imposing monetary penalties provided under Subsec. 4192Q.2 for delayed submission of reports, the amendments to the Plan shall be considered as *"Category A-3"* report. The amendments shall be deemed approved after thirty (30) business days from date of completion of requirements.

A copy of the Plan shall be available at the principal office of the trustee during regular office hours, for inspection by any person having an interest in the fund or by his authorized representative. Upon request, a copy of the Plan shall be furnished such interested person.

(As amended by Circular No. 593 dated 08 January 2008)

§ 4410Q.7 *Minimum disclosure requirements*

a. *Disclosure of UIT Fund investments*. A list of prospective and outstanding investment outlets shall be made available by the trustee for the review of all UIT Fund clients. Such disclosure shall be substantially in the form as shown in *Appendix Q-34*. The list of investment outlets shall be updated quarterly.

b. *Distribution of investment units* The trustee may issue such conditions or rules, as may affect the distribution of investment

units subject to the minimum conditions enumerated hereunder.

(1) *Marketing materials*. All printed marketing materials related to the sale of a UIT Fund shall clearly state:

(a) The designated name and classification of the fund and the fund's trustee.

(b) Minimum information regarding:

(i) The general investment policy and applicable risk profile. There shall be a clear description/explanation of the general risks attendant with investing in a UIT Fund, including risk specific to a type of fund. Technical terms should likewise be defined in laymen's terms[1].

(ii) Particulars or administrative and marketing details like pricing and cut-off time.

(iii) All charges made/to be made against the fund, including trust fees, other related charges.

(iv) The availability of the Plan rules governing the fund, upon the client's request.

(v) Client and Product Suitability Standards. Prior to admission, the trustee shall perform a client profiling process for all UIT Fund participants under the general principles on client suitability assessment to guide the client in choosing investment outlets that are best suited to his objectives, risk tolerance, preferences and experience. The profiling process shall, at the minimum, require the trustee to obtain client information through the Client Suitability Assessment (CSA) form, classify the client according to his financial sophistication and communicate the CSA results to the subject client. The general principles on CSA shall also require the trustee to adopt a notice mechanism whereby clients are advised and/or reminded of the explicit requirement to notify the trustee or its UIT Fund marketing personnel of any change in their characteristics, preferences or circumstances to enable the trustee to update client's profile at least every three (3) years.

(c) The participation is not a "deposit account" but a trust product; and that any loss/income is for the account of the participant; that the trustee is not liable for losses unless upon willful default, bad faith or gross negligence.

(d) A balanced assessment of the possible gains and losses of the UIT Fund and that the participation does not carry any guaranteed rate of return, and is not insured by the PDIC.

(e) An advisory that the investor must read the complete details of the fund in the Plan Rules, make his/her own risk assessment, and when necessary, he/she must seek independent/professional opinion, before making an investment.

(2) Evidence of participation. Every UIT Fund participant shall be given -

(a) A participating trust agreement. Such agreement shall clearly indicate that (1) the UIT Fund is a trust product and not a deposit account or an obligation of, or guaranteed, or insured by the trust entity or its affiliates or subsidiaries; (2) the UIT Fund is not insured or governed by the PDIC; (3) due to the nature of the investment, yields and potential yields cannot be guaranteed; (4) any loss/income arising from market fluctuations and price volatility of the securities held by the UIT Fund, even if invested in government securities, is for the account of the client/participant; (5) as such, the units of participation of the investor in the UIT Fund, when redeemed, may be worth more or be worth less than his/her initial investment/contributions; (6) historical performance, when presented, is purely for reference purposes and is not a guarantee of similar future result; and (7) the trustee is not liable for losses unless upon willful default, bad faith or gross negligence.

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[1] Example: "Fixed income securities" does not really mean a guarantee of fixed earnings on the investor's participation; "Risk-free" government securities which may be sovereign "risk-free" but not interest rate "risk-free".

In addition to the agreement, every UIT Fund participant shall be provided with –

(1) CSA form to be accomplished during the profiling process required under the general principles on CSA. This is designed to ensure that based on relevant information about the client, his investment profile is matched against the investment parameters of the UIT Fund. At the minimum, client information shall include personal or institutional data, investment objective, investment horizon, investment experience, and risk tolerance; and

(2) Risk disclosure statement, which in reference to Subsec. 4410Q.6c, shall describe the attendant general and specific risks that may arise from investing in the UIT Fund. Such statement shall be substantially similar to the form in *Annex A* of *Appendix Q-34a*.

Both documents shall be signed by the client/participant and the UIT marketing personnel who assessed and explained to the concerned client his/her ability to bear the risks and potential losses.

(b) A confirmation of participation and redemption made to/from the fund that shall contain the following information:

(i) NAVPu of the fund on day of purchase /redemption;

(ii) Number of units purchased/ redeemed; and

(iii) Absolute peso or foreign currency value.

No indicative rates of return shall be provided in the trust participating agreement. Marketing materials may present relevant historical performance purely for reference and with clear indication that past results do not guarantee similar future results.

(3) A participating trust agreement or confirmation of contribution/redemption need not be manually signed by the trustee or his authorized representative if the same is in the form of an electronic document that conforms with the implementing rules and regulations of R.A. No. 8792, otherwise known as the E-Commerce Act.

c. *Regular publication/computation/ availability of the fund's* NAVPu. Trust entities managing a UIT Fund shall cause at least the weekly publication of the NAVPu of such fund in one (1) or more newspaper of national circulation: *Provided*, That a pooled weekly publication of such NAVPu shall be considered as substantial compliance with this requirement. The said publication, at the minimum, shall clearly state the name of the fund, its general classification, the fund's NAVPu and the moving return on investment (ROI) of the fund on a year-to-date (YTD) and year-on-year (YOY) basis.

NAVPu shall be computed daily and shall be made available to participants and prospective participants upon request.

d. *Marketing personnel*. To ensure the competence and integrity of all duly designated UIT marketing personnel, all personnel involved in the sales of these funds shall be required to undergo standardized training program in accordance with the guidelines of this Subsection. This training program may be conducted by their respective trust entities in accordance with the minimum training program guidelines provided by the Trust Officers Association of the Philippines (TOAP). Such training program shall however be regularly validated by TOAP.
(As amended by Circular No. 593 dated 08 January 2008)

§ 4410Q.8 *Exposure limit to single person/entity.* The combined exposure of the UIT Fund to any entity and its related parties shall not exceed fifteen percent (15%) of the market value of the UIT Fund: *Provided,* That, a UIT Fund invested, partially or substantially, in exchange traded equity securities shall be subject to the fifteen percent (15%) exposure limit to a single entity/issuer: *Provided, further,*

That, in the case of an exchange traded equity security which is included in an index and tracked by the UIT Fund, the exposure of the UIT Fund to a single entity shall be the actual benchmark weighting of the issuer or fifteen percent (15%), whichever is higher.

This limitation shall not apply to non-risk assets as defined by the BSP.

In case the limit is breached due to the marking-to-market of certain investment/*s* or any extraordinary circumstances, *e.g.*, abnormal redemptions which are beyond the control of the trustee, the trustee shall be given thirty (30) days from the time the limit is breached to correct the same.

(As amended by Circular No. 577 dated 17 August 2007)

§ 4410Q.9 *Allowable investments and valuation.* UITF investments shall be limited to bank deposits and the following financial instruments:

(a) Securities issued by or guaranteed by the Philippine government, or the BSP;

(b) Tradable securities issued by the government of a foreign country, any political subdivision of a foreign country or any supranational entity;

(c) Exchange-listed securities;

(d) Marketable instruments that are traded in an organized exchange;

(e) Loans traded in an organized market;

(f) Loans arising from repo agreements which are transacted through an exchange recognized by the SEC, subject to the condition that the repo contracts may be pre-terminated lawfully by the trust entity administering the UITF and acting as lender, with due notice to its counterparty and the market operator; and

(g) Such other tradable investments outlets/categories as the BSP may allow.

Provided, That the investment of the peso UITF in tradable foreign currency-denominated financial instruments shall be subject to Items *"e"* and *"f"* of Subsec. 4409Q.6.

Provided further, That a financial instrument is regarded as tradable if quoted two-way prices are readily and regularly available from an exchange, dealer, broker, industry group, pricing service or regulatory agency, and those prices represent actual and regularly occurring market transactions on an arm's length basis.

The UITF may avail itself of financial derivatives instruments solely for the purpose of hedging risk exposures of the existing investments of the Fund, provided these are accounted for in accordance with existing BSP hedging guidelines as well as the trust entity's risk management and hedging policies duly approved by the Trust Committee and disclosed to participants.

The use of hedging instruments shall also be disclosed in the "Plan" as provided in Item *"c"* of Subsec. 4410Q.6 and specified in the quarterly "list of investment outlets" as provided in Item *"a"* of Subsec. 4410Q.7.

(As amended by M-2010-033 dated 04 October 2010, Circular Nos. 676 dated 29 December 2009 and 675 dated 22 December 2009)

§ 4410Q.10 *Other related guidelines on valuation of allowable investments*

a. In pricing debt securities, interpolated yields shall be used for securities with odd or off-the-run tenors using the straight-line basis and generally accepted market convention.

b. In case outstanding UIT Fund investments may deteriorate in quality, i.e., no longer tradable as defined under Subsec. 4410Q.9, the trustee shall immediately provision to reflect fair value in accordance with generally accepted accounting principles or as may be prescribed by the BSP. If no fair value is available, the instrument shall be assumed to be of no market value.

§ 4410Q.11 ***Unit investment trust fund administration support***

a. *Backroom operations*. Administrative rules on backroom under Sec. 4421Q shall be applicable to UIT Fund. Adequate systems to support the daily marking-to-market of the fund's financial instruments shall be in place at all times. In this respect, a daily reconcilement of the fund's resultant marked-to-market value with the unrealized market losses and gains (respective contra asset balance) versus the book value of the fund for investments in financial instruments shall be done and all differences resolved within the day.

b. *Custody of securities*. Investments in securities of a UIT Fund shall be held for safekeeping by BSP accredited third party custodians which shall perform independent marking-to-market of such securities.

§ 4410Q.12 ***Counterparties***

a. *Dealings with related interests/QB proper/holding company/subsidiaries/ affiliates and related companies*. A trustee of a UIT Fund shall be transparent at all times and maintain an audit trail for all transactions with related parties or entities. The trustee shall observe the principle of best execution and no purchase/sale shall be made with related counterparties without considering at least two (2) competitive quotes from other sources.

b. *Accreditation of counterparties* The Fund shall only invest with approved counterparties qualified in accordance with the policy duly approved by the Trust Committee. Counterparties shall be subject to appropriate limits in accordance with sound risk management principles.

§ 4410Q.13 ***Foreign currency-denominated unit investment trust funds*** UIT Fund denominated in any acceptable foreign currency provided under existing BSP rules and regulations may be established. Such fund may only be invested in allowable investments denominated in pesos or any acceptable foreign currency as expressly allowed under the fund's Plan rules and properly disclosed to fund participants.

§ 4410Q.14 ***Exemptions from statutory and liquidity reserves, single borrowers limit, directors, officers, stockholders and their related interest.*** The provisions on reserves, single borrower's limit and DOSRI ceilings under Secs. 4330Q and 4331Q, respectively, applicable to trust funds in general shall not be made applicable to UIT Funds.

Sec. 4411Q Investment Management Activities. The conduct of investment management activities shall be subject to the following regulations.

§ 4411Q.1 ***Minimum documentary requirements.*** An investment management account (IMA) shall be covered by a written document establishing such account, as follows:

a. In the case of accounts created by corporations, business firms, organizations or institutions, the voluntary written agreement or indenture entered into by the parties, accompanied by a copy of the board resolution or other evidence authorizing the establishment of, and designating the signatories, to the investment management account.

b. In the case of accounts created by individuals, the voluntary written agreement or indenture entered into by the parties.

The voluntary written agreement or contract shall include the following minimum provisions:

(1) Prenumbered contractual agreement form;

(2) Title or nature of contractual agreement in noticeable print;

(3) Legal capacities, in noticeable print, of parties sought to be covered;

(4) Purposes and objectives;

(5) The initial amount of funds and/or value of securities subject of the arrangement delivered to the investment manager;

(6) Statement in underlined noticeable print that:

(a) The agreement is an agency and not a trust agreement. As such, the client shall at all times retain legal title to funds and properties subject of the arrangement;

(b) The arrangement does not guaranty a yield, return or income by the investment manager. As such, past performance of the account is not a guaranty of future performance and the income of investments can fall as well as rise depending on prevailing market conditions; and

(c) The investment management agreement is not covered by the PDIC and that losses, if any, shall be for the account of the client;

(7) Duties and powers of the investment manager;

(8) Liabilities of the investment manager;

(9) Reports to the client;

(10) The amount or rate of the compensation of the investment manager;

(11) Terms and conditions governing withdrawals from the account;

(12) Termination of contractual arrangement; and

(13) Disclosure requirements for transactions requiring prior authority and/or specific written investment directives from the client.

A sample investment management agreement which conforms to the foregoing requirements is shown as *Appendix Q-14*.

§ 4411Q.2 ***Minimum size of each investment management account.*** No IMA shall be accepted or maintained for an amount less than P1.0 million. An IMA reduced to less than P1.0 million due to investment losses shall be exempt from this requirement.

§ 4411Q.3 ***Commingling of funds*** Two (2) or more individual IMAs shall not be commingled except for the purpose of investing in government securities or in duly registered commercial papers: *Provided,* That the participation of each of the aforementioned accounts in the commingled account shall not be less than P1 million: *Provided, further,* That such commingling has been fully disclosed and specifically agreed in writing by the clients.

§ 4411Q.4 ***Lending and investment disposition.*** Assets received in investment management capacity shall be administered in accordance with the terms of the instrument creating the investment management relationship.

When an investment manager is granted discretionary powers in the investment disposition of investment management funds and unless otherwise specifically enumerated in the agreement or indenture and directed in writing by the client, loans and investments of the fund shall be limited to:

a. Evidences of indebtedness of the Republic of the Philippines and of the BSP, and any other evidences of indebtedness or obligations the servicing and repayment of which are fully guaranteed by the Republic of the Philippines or loans against such government securities;

b. Loans fully guaranteed by the Republic of the Philippines as to the payment of principal and interest;

c. Loans fully secured by a hold-out on, assignment or pledge of deposit substitutes maintained with the institution or deposits with banks, or mortgage and chattel mortgage bonds issued by the investment manager; and

d. Loans fully secured by real estate or chattels in accordance with Section 78 of

R.A. No. 337, as amended, and subject to the requirements of Sections 75, 76 and 77 of R.A. No. 337, as amended.

The specific directives required under this Subsection shall consist of the following information:

(1) The transaction to be entered into;
(2) Borrower's name;
(3) Amount involved; and
(4) Collateral security(ies), if any.

§ 4411Q.5 ***Transactions requiring prior authority.*** An investment manager shall not undertake any of the following transactions for the account of a client, unless prior to its execution, such transaction has been fully disclosed and specifically authorized in writing by the client:

a. Lend, sell, transfer or assign money or property to any of the departments, directors, officers, stockholders, or employees of the investment manager, or relatives within the first degree of consanguinity or affinity, or the related interests of such directors, officers and stockholders; or to any corporation where the investment manager owns at least fifty percent (50%) of the subscribed capital or voting stock in its own right and not as trustee nor in a representative capacity;

b. Purchase or acquire property or debt instruments from any of the departments, directors, officers, stockholders, or employees of the investment manager, or relatives within the first degree of consanguinity or affinity, or the related interests of such directors, officers and stockholders; or from any corporation where the investment manager owns at least fifty percent (50%) of the subscribed capital or voting stock in its own right and not as trustee nor in a representative capacity;

c. Invest in equities of or in securities underwritten by the investment manager or a corporation in which the investment manager owns at least fifty percent (50%) of the subscribed capital or voting stock in its own right and not as trustee, nor in a representative capacity; and

d. Sell, transfer, assign or lend money or property from one trust fiduciary or IMA to another trust, fiduciary or IMA except where the investment is in any of those enumerated in Items *"a"* to *"d"* of Subsec. 4411Q.4.

Directors, officers, stockholders and their related interest covered by this Subsection shall be those considered as such under existing regulations on loans to DOSRI under Part III - E of this Manual. The procedural and reportorial requirements in said regulations shall also apply.

The disclosure required under this Subsec. shall consist of the following minimum information:

(1) The transactions to be entered into;
(2) Identities of the parties involved in the transaction and their relationships (shall not apply to Item *"d"* of this Subsec.);
(3) Amount involved; and
(4) Collateral security(ies), if any.

The above information shall be made known to clients in a separate instrument or in the very instrument creating the investment management relationship.

§ 4411Q.6 ***Title to securities and other properties.*** Securities such as promissory notes, shares of stocks, bonds and other properties of the portfolio shall be issued or registered in the name of the principal or of the investment manager: *Provided,* That in case of the latter, the instrument shall indicate that the investment manager is acting in a representative capacity and that the principal's name is disclosed thereat.

§ 4411Q.7 ***Ceilings on loans.*** Loans funded by IMAs shall be subject to the DOSRI ceilings imposed on QBs in Part III - E of this Manual. For purposes of determining compliance with said ceilings, the total amount of said loans granted by the institution and its trust department to

the same person, firm or corporation shall be combined.

§ 4411Q.8 ***Other applicable regulations on loans and investments - investment management account.*** The loans and investments of IMAs shall be subject to pertinent laws, rules and regulations for QBs that shall include, but need not be limited to, the following:

a. Requirements of Sections 39 and 40 of R.A. No. 8791 (The General Banking Law of 2000);

b. Provisions of Section 4(e) of the New Rules on Registration of Short-Term Commercial Papers and Section 7(f) of the New Rules on Registration of Long-Term Commercial Papers issued by the SEC *(Appendices 13* and *14)*;

c. Criteria for past due accounts;

d. Qualitative appraisal of loans, investments and other assets that may require provision for probable losses which shall be booked in accordance with the FRPTIs;

e. Requirements of Sections 3 and 8 of the SRC; and

f. Provisions of Section 44 – Investments by Philippine Residents – of the FX Manual, such that the cross-currency investments of peso IMAs, shall be subject to the following conditions:

(1) All cash flows of the investment manager shall only be in pesos. In case the foreign exchange acquired or received by the principal as dividends/earnings or divestment proceeds on such investment are intended for reinvestment abroad, the same proceeds are not required to be inwardly remitted and sold for pesos through authorized agent banks: *Provided*, That such proceeds are reinvested abroad within two (2) banking days from receipt of the funds abroad;

(2) The investment manager shall purchase, invest, reinvest, sell, transfer or dispose foreign currency-denominated financial instruments, including securities as defined in Section 3 of the SRC, through a distributor or underwriter duly authorized or licensed by the government of the issuer of such instruments, or a counterparty FI (seller or buyer) authorized in writing by the principal and/or accredited by the investment manager: *Provided*, That, the conduct, documentation, and settlement of any of these transactions shall be outside Philippine jurisdiction;

(3) The investment manager shall record cross-currency investment transactions in the peso regular books at their foreign currency amounts and their local currency equivalent using the Philippine Dealing System peso/US dollar closing rate and the New York US dollar/ third currencies closing rate; and

(4) The investment manager shall comply with the reportorial requirements that may be prescribed by the BSP, which shall include as a minimum, the foreign currency amount and the local currency equivalent of the total cross currency investments with details on: (a) type of investments; and (b) amount of cash flow converted.

For purposes of this Subsection, *"resident"*, as defined under Section 1 of the FX Manual, shall refer to the principal that engages the services of the investment manager under an investment management agreement.

(Circular No. 676 dated 29 December 2009)

§ 4411Q.9 ***Operating and accounting methodology.*** IMAs shall be operated and accounted for in accordance with the following:

a. The investment manager shall administer, hold or manage the fund or property in accordance with the instrument creating the investment management relationship; and

b. Funds or property of each client shall be accounted separately and distinctly from those of other clients herein referred to as *individual account accounting*.
(As amended by Circular No. 676 dated 29 December 2009)

§ 4411Q.10 *Tax-exempt individual investment management accounts*. The following shall be the features/requirements of IMAs of individuals which may be exempted from the twenty percent (20%) final tax under Section 24(B)(1) of R.A. No. 8424 (The Tax Reform Act of 1997):

a. The tax exemption shall apply to investment management agreements contracted on or after 03 January 2000;

b. The investment management agreement shall only be between individuals who are Filipino citizens or resident aliens and investment manager banks. The agreement shall be non-negotiable and non-transferable;

c. The minimum amount of investment for an IMA shall be P1.0 million;

d. The investment management agreement shall indicate that pursuant to Section 24(B)(1) of R.A. No. 8424, interest income of the investment management funds derived from investments in interest-bearing instruments (e.g., time deposits, government securities, loans and other debt instruments) which are otherwise subject to the twenty percent (20%) final tax, shall be exempt from said final tax provided the funds are held under investment management by the investment manager for at least five (5) years. If said funds are held by the investment manager for a period less than five (5) years, interest income shall be subject to a final tax which shall be deducted and withheld from the proceeds of the IMA based on the following schedule–

Holding Period	Rate of Tax
Four (4) years to less than five (5) years	5%
Three (3) years to less than four (4) years	12%
Less than three (3) years	20%

Necessarily, the investment management agreement shall clearly indicate the date when the investment manager actually received the funds which shall serve as basis for determining the holding period of the funds;

e. The investment manager may accept additional funds for inclusion in IMAs which have been established as tax-exempt under R.A. No. 8424. However, the receipt of additional funds shall be properly documented by indicating that they are part of existing tax-exempt IMAs and that the interest income of the additional funds derived from investments in interest bearing instruments shall be exempt from the twenty percent (20%) final tax under the same conditions mentioned in the preceding item. The document shall also indicate the date when the additional funds were received by the investment manager bank to serve as basis for determining the minimum five (5)-year holding period for tax exemption purposes of the additional funds; and

f. Tax-exempt individual IMAs established under this Subsection shall be subject to the provisions of Subsecs. 4411Q.1(b) and 4411Q.2 up to 4411Q.8.

Sec. 4412Q (Reserved)

Sec. 4413Q Required Retained Earnings Appropriation. An institution authorized to engage in trust and other fiduciary business shall, before the declaration of dividends, carry to retained earnings appropriated for trust business at least ten percent (10%) of its net profits realized out of its trust, investment management and other fiduciary business since the last preceding dividend declaration until the retained earnings shall amount to twenty percent (20%) of its authorized capital stock and no part of such retained earnings shall at any time be paid out in dividends but losses accruing in the course of its business may be charged against surplus.

B. INVESTMENT MANAGEMENT ACTIVITIES

Sec. 4414Q Authority to Perform Investment Management. An IH may act as financial consultant, investment adviser or portfolio manager under Section 7 of P.D. No. 129, as amended. However, this shall not be construed as authority to engage in trust and other fiduciary business. Entities whose articles of incorporation[1] or any amendments thereto, include the purpose or power to act as financial consultant, investment adviser or portfolio manager shall secure the prior favorable recommendation of the Monetary Board before the filing of said articles of incorporation or amendments thereto with the SEC.

If an entity is found to be engaged in unauthorized investment management activities, whether as its primary, secondary or incidental business, the Monetary Board may impose administrative sanctions against such entity or its principal officers and/or majority stockholders or proceed against them in accordance with law.

The Monetary Board may take such action as it may deem proper such as, but may not be limited to, requiring the transfer or turnover of any IMA to duly incorporated and licensed entities of the choice of the client.

An entity not authorized to engage in investment management activities shall not advertise or represent itself as being engaged in investment management activities or represent itself as investment manager or use words of similar import.

Starting year 2001, IHs authorized to engage in investment management activities shall renew their existing licenses yearly, subject to the implementing guidelines to be issued thereon.

(As amended by CL-2008-078 dated 15 December 2008, CL-2008-053 dated 21 August 2008 and CL-2008-007 dated 21 January 2008)

§ 4414Q.1 ***Prerequisites for engaging in investment management activities.*** An entity before it may engage in investment management activities shall comply with the following requirements:

a. It has been duly licensed by the appropriate government agency or created by special law or charter.

b. The articles of incorporation or charter of the institution shall include among its powers or purposes the authority to engage in investment management activities.

c. The by-laws of the institution shall include, among other things:

(1) The organization plan or structure of the department, office or unit which shall conduct the investment management activities of the institution;

(2) The creation of an investment management committee, the appointment of an investment management officer and subordinate officers of the investment management department; and

(3) A clear definition of the duties and responsibilities, as well as the line and staff functional relationships, of the various units, officers and staff within the organization.

d. Where the applicant is authorized to engage in quasi-banking functions, the applicant shall also meet the following additional requirements:

(1) It has continuously complied with the capital-to-risk assets ratio, reserve requirements against deposit substitutes, liquidity floor, and ceilings on DOSRI loans for the last sixty (60) days immediately preceding the date of application;

(2) It has not incurred net weekly reserve deficiencies against deposit substitutes during the last eight (8) weeks immediately preceding the date of application; and

(3) It has shown substantial compliance with other pertinent laws, rules and regulations, policies and instructions of the BSP and has not been cited for serious/

[1] SEC Memorandum Circular Nos. 5 dated 17 July 2008, 3 dated 16 February 2006 and 14 dated 24 October 2000.

major violations or exceptions affecting its solvency, liquidity and profitability.

Where the applicant is not authorized to engage in quasi-banking functions:

(a) The adoption of a formula/criteria for QBs in the determination of compliance with the capital-to-risk assets ratio and ceilings on loans to DOSRI; and

(b) The substitution of the reserve and liquidity floor requirements with the cash ratio, as follows:

(i) Primary reserves to Bills Payable; and

(ii) Primary and secondary reserve to Bills Payable:

where primary reserves consist of cash on hand, cash in vault, checks and other cash items, due from the BSP and due from banks; and where secondary reserves consist of BSP-supported government securities, T- Bills and other government securities.

Compliance with the foregoing, as well as with other requirements under existing regulations, shall be maintained up to the time the authority is granted. An applicant that fails in this respect shall be required to show compliance for another test period of the same duration.

§ 4414Q.2 *Pre-operating requirements*
An institution authorized to engage in investment management activities shall, before engaging in actual operations, submit to the BSP the following:

a. Government securities acceptable to the BSP amounting to P500,000 as minimum basic security deposit for the faithful performance of investment management duties required under Subsec. 4415Q.1;

b. Organization chart of the investment management department which shall carry out the investment management activities of the institution; and

c. Names and positions of individuals designated as chairman and members of the investment management committee, investment management officer and other subordinate officers of the investment management department.

Sec. 4415Q Security for the Faithful Performance of Investment Management Activities

§ 4415Q.1 *Basic security deposit*
An institution authorized to engage in investment management activities shall deposit with the BSP eligible government securities as security for the faithful performance of its investment management activities equivalent to at least one percent (1%) of the book value of the total volume of investment management assets: *Provided,* That at no time shall such deposit be less than P500,000.

Scripless securities under the RoSS system of the BTr may be used as basic security deposit for the faithful performance of investment management activities using the guidelines in *Appendix Q-21*.

§ 4415Q.2 *Eligible securities.* Securities enumerated in Subsec. 4405Q.2 shall be eligible as security deposit for faithful performance of investment management activities.

§ 4415Q.3 *Valuation of securities and basis of computation of the basic security deposit requirement.* For purposes of determining compliance with the basic security deposit under this Section, the amount of securities so deposited shall be based on their book value, that is, cost as increased or decreased by the corresponding discount or premium amortization.

The base amount for the basic security deposit shall be the average of the month-end balances of the total assets of investment management funds of the immediately preceding calendar quarter.

§ 4415Q.4 ***Compliance period; sanctions.*** The investment manager shall have thirty (30) calendar days after the end of every calendar quarter within which to deposit with the BSP securities required under this Section.

The following sanctions shall be imposed for any deficiency in the basic security deposit for the faithful performance of investment management activity:

a. On the QB:

i. Monetary penalty/ies:

Penalty per Calendar Day	QBs with Full Trust Authority and with Trust Assets of (Trust Asset Size \ Offense)	First	Second	Third and subsequent offense(s)
	Up to P500 million	P600.00	P700.00	P800.00
	Above P500 million but not exceeding P1 billion	P1,000.00	P1,250.00	P1,500.00
	Above P1 billion but not exceeding P10 billion	P2,000.00	P3,000.00	P4,000.00
	Above P10 billion but not exceeding P50 billion	P5,000.00	P6,000.00	P7,000.00
	Above P50 billion	P8,000.00	P9,000.00	P10,000.00

ii. Non-monetary penalty beginning with the third offense (all QBs) - Prohibition against the acceptance of new IMAs, and from renewing expiring investment management contracts up to the time the violation is corrected.

b. On the Head of the Investment Management Department and/or other officer(s) responsible for the deficiency/ non-compliance:

(1) *First offense* - warning that subsequent violations shall be dealt with more severely;

(2) *Second offense* - written reprimand with a stern warning that subsequent violations shall be subject to suspension;

(3) *Third offense* - thirty (30) calendar day-suspension without pay; and

(4) *Subsequent offense(s)* - sixty (60) calendar day-suspension without pay.

For purpose of determining the frequency of the violation the QB's compliance profile for the immediately preceding three (3) years or twelve (12) quarters will be reviewed: *Provided*, That for purposes of determining appropriate penalty on the head of the Investment Management Department and/or other responsible officer(s), any offense committed outside the preceding three (3) year or twelve (12) quarter-period shall be considered as the first offense: *Provided, further,* That in the case of the head of the Investment Management Department, all offenses committed by him in the past as the head of the Investment Management Department of other institution(s) shall also be considered: *Provided, finally,* That if the offense cannot be attributed to any other officer of the QB, the head of the Investment Management Department shall be automatically held responsible since the ultimate responsibility for ensuring compliance with the regulation rests upon him, as evidence may warrant.

(As amended by Circular Nos. 617 dated 30 July 2008 and 585 dated 15 October 2007)

Sec. 4416Q Organization and Management

The provisions under Sec. 4406Q up to Subsec. 4406Q.9 shall govern the organization and management of institutions without trust license which are engaged in investment management activities only. The following terms shall, however, be used:

a. Investment management activities in lieu of trust and other fiduciary business;

b. IMAs in lieu of trust and other fiduciary accounts;

c. Investment management committee in lieu of trust committee;

d. Investment management officer in lieu of trust officer; and

e. Investment management department in lieu of trust department.

(As amended by M-2007-009 dated 22 March 2007)

Sec. 4417Q Non-Investment Management Activities. The provisions of Sec. 4407Q shall apply in determining non-investment management activities except that the terms *trust, other fiduciary, trustee* and *fiduciary* shall be disregarded.

Sec. 4418Q Unsound Practices. The provisions of Sec. 4408Q shall govern the unsound practices for IMAs.

Sec. 4419Q Conduct of Investment Management Activities. The provisions of Sec. 4411Q shall govern the conduct of investment management activities of an institution without trust license that is engaged in investment management activities.

Sec. 4420Q Required Retained Earnings Appropriation. An institution authorized to engage in investment management activities shall, before the declaration of dividends, carry to retained earnings appropriated for trust business at least ten percent (10%) of its net profits realized out of its investment management activities since the last preceding dividend declaration until the retained earnings shall amount to twenty percent (20%) of its authorized capital stock and no part of such retained earnings shall at any time be paid out in dividends, but losses accruing in the course of its business may be charged against retained earnings.

C. GENERAL PROVISIONS

Sec. 4421Q Books and Records. The institution's trust department or investment management department shall keep books and records on trust, other fiduciary and IMAs separate and distinct from the books and records of its other businesses and shall follow the FRPTI prescribed by the BSP.

Each trust, other fiduciary or IMA shall have a record separate from all other accounts except only in the case of CTFs where the trustee can maintain common records utilizing *pooled fund accounting* method for each fund: *Provided,* That the trustee shall clearly indicate in the records the trustors owning participation in the CTF and the extent of the interest of such trustors.

Books and records shall contain full information relative to each trust, other fiduciary or IMA and shall be supported by duplicate signed copies of related documents. Said records and duplicate signed copies or related documents shall be compiled and kept as to allow inspection by BSP examiners and submission of information or reports as may be required by competent authorities.

The QB's trust department or investment management department shall maintain separate general ledger accounts and other relevant sub-accounts for tax-exempt individual trust accounts, CTFs and individual management accounts established under Section 24(B)(1) of R.A. No. 8424 and Subsecs. 4409.8, 4411.9, and Item *"8"* of *Appendix Q-32*. The bank's trust department or investment management department shall also adopt appropriate systems, internal control procedures and audit trail mechanisms to ensure that the correct amount of final tax is withheld or exempted from such accounts.

(As amended by Circular No. 653 dated 05 May 2009)

Sec. 4422Q Custody of Assets. All monies, properties or securities received by an institution in its capacity as trustee, fiduciary, or investment manager shall be kept physically separate and distinct from the assets of its other businesses and shall be under the joint custody of at least two (2) persons, one of whom shall be an officer of the trust or investment management department, designated for that purpose by the board of directors.

The investment of each trust, other fiduciary or IMA shall be kept physically separated from those of other trust, other fiduciary or IMAs, and adequately identified as the assets or property of the relevant account.

Sec. 4423Q Fees and Commissions. An institution acting as trustee, fiduciary or investment manager shall be entitled to reasonable fees and commissions which shall be determined on the basis of the cost of services rendered and the responsibilities assumed: *Provided,* That where the trustee, fiduciary or investment manager is acting as such under appointment by a court, the compensation shall be that allowed or approved by the court: *Provided, further,* That in the case of CTFs, the fee which a trustee may charge each participant shall be fully disclosed by the trustee in the CTF plan, prospectus, flyers, posters and all forms of advertising materials to market the fund and in the documents given to clients as proof of participation in the fund. In no case shall such fees and commissions be based on the excess of the income of the trust, other fiduciary or investment management funds over a certain amount or percentage.

No trustee, fiduciary or investment manager shall solicit or receive rebates on commissions, fees and other payments for the services rendered to the trust, other fiduciary or IMA or beneficiaries of the trust, other fiduciary or IMA by stockbrokers, real estate brokers, insurance agents and similar persons or entities unless the rebates, fees and other payments shall accrue to the benefit of the trust, other fiduciary or IMA or the beneficiaries thereof.

Officers and employees of the trust department or investment management department of institutions, while serving as such, shall be prohibited from retaining any compensation for acting as co-trustee or fiduciary in the administration of a trust, other fiduciary or IMA.

No institution shall collect, for its own account, referral and/or arrangement fees, or any other fees that take the nature of payment to the institution from whatever source, in connection with loans sourced from trust funds managed by its trust department: *Provided,* That if such fees are collected, the same shall be properly disclosed to the trustor, and shall accrue to the benefit of the trust, in accordance with the provisions of Secs. 4401Q and 4407Q.

(As amended by Circular No. 541 dated 30 August 2006)

Sec. 4424Q Taxes. The terms and conditions of trust, other fiduciary or investment management agreements, including CTF plans, shall contain provisions regarding the applicability of regulations governing taxation on the income of trust, other fiduciary or investment management accounts. For this purpose, the trustee, fiduciary or investment manager shall maintain adequate records and shall include information such as the amount of final income tax withheld at source and the amount withheld by the trustee, fiduciary or investment manager in the periodic reports submitted to trustors, beneficiaries, principals and other parties in interest.

With respect to tax-exempt CTFs, individual trust and investment management accounts established under Section 24(B)(1) of R.A. No. 8424, the bank's trust department or investment management department shall be responsible for

obtaining the tax-exemption certifications which may be required by the BIR for the interest-bearing instruments where the CTFs, individual trust funds and investment management funds will be invested. Likewise, the banks shall ensure that the correct amount of final tax on the interest income on the interest-bearing instruments is withheld/deducted from the proceeds from the CTF participation, trust or investment management account and remitted to the BIR in the event said tax becomes due such as when funds are withdrawn before the required five (5)-year holding period or when corporations happen to invest in the tax-exempt trust instruments created within the purview of R.A. No. 8424.

Sec. 4425Q Reports Required

§ 4425Q.1 ***To trustor, beneficiary, principal.*** Every institution acting as trustee, fiduciary or investment manager shall render reports on the trust, other fiduciary or IMAs to the trustor, beneficiary, principal or other party in interest or the court concerned or any party duly designated by the court order, as the case may be, under the following guidelines:

a. The reports shall be in such forms as to apprise the party concerned of the significant developments in the administration of the account and shall consist of:

(1) A balance sheet;
(2) An income statement;
(3) A schedule of earning assets of the account; and
(4) An investment activity report;

b. Items *(3)* and *(4)* above shall include at least the following:

(1) Name of issuer or borrower;
(2) Type of instrument;
(3) Collateral, if any;
(4) Amount invested;
(5) Earning rate or yield;
(6) Amount of earnings;
(7) Transaction date; and
(8) Maturity date;

c. The reports shall be prepared in such frequency as required under the agreement but shall not in any case be longer than once every quarter; and

d. The reports shall be made available to clients not later than twenty (20) calendar days from the end of the reference date/ period in Item *"c"* above.

§ 4425Q.2 ***To the Bangko Sentral*** An institution acting as trustee, fiduciary or investment manager shall submit periodic reports prescribed by the appropriate department of the SES on the institution's trust and other fiduciary business and investment management activities within the deadline indicated in *Appendix Q-3*.

§ 4425Q.3 ***Audited financial statements*** The trust/investment management department of an institution shall adopt the provisions of the Philippine Financial Reporting Standards (PFRS)/Philippine Accounting Standards (PAS) in all respect, for purposes of preparing the AFS of its trust and other fiduciary and investment management activities. The following guidelines shall likewise be observed in the preparation of the AFS:

(a) The provisions of PFRS/PAS shall be adopted effective the annual financial statements beginning 01 January 2008;

(b) A complete set of financial statements shall comprise of the following:

(1) Balance sheet as of the end of the period;
(2) Income statement for the period;
(3) Statement of changes in accountabilities, which shall show a reconciliation of the net carrying amount at the beginning and end of the period of the following accounts:
(i) principal;
(ii) accumulated income; and

(iii) net unrealized gains/(losses) on available for sale financial assets, separately disclosing the changes in each of the foregoing accounts;

(4) Notes, which shall comprise of a summary of significant accounting policies and other disclosure requirements provided under PFRS/PAS: *Provided,* That for purposes of complying with the disclosure of the nature and extent of risks arising from financial instruments as required under PFRS 7, disclosure statements may be made based on the general categories of contractual relationships (i.e., UITF-trust, institutional-trust, and individual-trust; other fiduciary; institutional-agency, and individual-agency; and special purpose trust) of the trust/investment management department of a bank with its clients; and

(5) Balance sheet as at the beginning of the earliest comparative period when a trust/investment management department applies an accounting policy retrospectively or when it makes a retrospective restatement of items in the financial statements, or when it reclassifies items in the financial statements.

(c) The balance sheet, income statement and statement of changes in accountabilities shall be presented for each of the general categories of contractual relationships (i.e., UITF-trust, institutional-trust, and individual-trust; other fiduciary; institutional-agency, and individual-agency; and special purpose trust) of the trust/investment management department of an institution with its clients;

(d) Comparative information for periods before 01 January 2008 need not be presented in the AFS for the financial reporting period beginning 01 January 2008: *Provided,* That disclosure statements on the end-2007 balances of total assets of the general categories of contractual relationships of the trust/investment management department of an institution with its clients prepared based on the Generally Accepted Accounting Principles (GAAP) previously applied, shall be presented in the notes to financial statements: *Provided, further*, That comparative periods shall be presented in the AFS for the financial reporting period beginning 01 January 2009 and thereafter.

(e) The following transitory rules and regulations shall govern the accounting treatment of specific items for purposes of preparing the AFS for the financial reporting period beginning 01 January 2008:

(1) The provisions of PFRS/PAS shall only be applied to accounts outstanding as of end-December 2008;

(2) Reclassification of previously recognized financial instruments shall no longer be allowed except as allowed under existing regulations; and

(3) The fair value of ROPA and Investment Properties as of the date of transition to PFRS/PAS may be used as the deemed cost of said properties as of that date: *Provided,* That said ROPA and Investment Properties shall be subsequently accounted for in accordance with the provisions of the FRPTI.

(Circular No. 653 dated 05 May 2009)

Sec. 4426Q Audits

§ 4426Q.1 *Internal audit.* The institution's internal auditor shall include among his functions, the conduct of periodic audits of the trust department or investment management department at least once every twelve (12) months. The board of directors, in a resolution entered in its minutes, may also require the internal auditor to adopt a suitable continuous audit system to supplement and/or to replace the periodic audit. In any case, the audit shall ascertain whether the institution's trust and other fiduciary business and investment management activities have been administered in accordance with laws, BSP rules and regulations, and sound trust or fiduciary principles.

§ 4426Q.2 *External audit.* The trust and other fiduciary business and investment management activities of an institution shall be included in the annual financial audit by independent external auditors required under Sec. 4190Q.

The audit of the assets and accountabilities of the trust department/ investment management department of an NBFI authorized to engage in trust and other fiduciary business/investment management activities, which shall cover at the minimum a review of the trust/ investment management operations, practices and policies, including audit and internal control system, shall be subject to auditing standards to the extent necessary to express an opinion on the financial statements.

The audit of the trust/investment management department of an institution authorized to engage in trust and other fiduciary business/investment management activities shall be covered by a separate supplemental audit report to be submitted to the institution's board of directors and to the BSP within the prescribed period containing, among other things, the complete set of financial statements of the trust/investment management department of an institution prepared in accordance with the provisions of Subsec. 4426Q together with the other information required by the BSP to be submitted under Sec. 4190Q: *Provided,* That a reconciliation statement of the balance sheet in the AFS and the FRPTI shall be prepared for each of the general categories of contractual relationships (i.e., UITF-trust, institutional-trust, and individual trust; other fiduciary; institutional-agency, and individual-agency; and special purpose trust) of the trust/investment management department of an institution with its clients following the format in *Appendix Q-50*.

(As amended by Circular No. 653 dated 05 May 2009)

§ 4426Q.3 *Board action.* A report of the foregoing audits, together with the actions thereon, shall be noted in the minutes of the board of directors of the institution.

Sec. 4427Q Authority Resulting from Merger or Consolidation. In merger of FIs, the authority to engage in trust and other fiduciary business and in investment management activities shall continue to be in effect if the surviving institution has such authority and the same has not been withdrawn by the BSP. In case the surviving institution does not have previous authority but desires to engage in trust and other fiduciary business and in investment management activities, it shall secure the prior approval of the Monetary Board to engage in such business as part of its application for merger to enable it to incorporate such among its powers or purpose clause in its articles of incorporation, articles of merger, by-laws and such other pertinent documents.

In the consolidation of FIs where the resulting entity is an entirely new one, it shall secure from the Monetary Board an authority to engage in trust and other fiduciary business or in investment management activities before it may engage in such business.

Sec. 4428Q Receivership. Whenever a receiver is appointed by the Monetary Board for an institution that is authorized to engage in trust and other fiduciary business or in investment management activities, the receiver shall, pursuant to the instructions of the Monetary Board, proceed to close the trust, other fiduciary and IMAs promptly and/or transfer all other accounts to substitute trustees, fiduciaries or investment managers acceptable to the trustors, beneficiaries, principals or other parties in interest: *Provided,* That where the trustee, fiduciary or investment manager is acting

as such under appointment by a court, the receiver shall proceed pursuant to the instructions of said court.

Sec. 4429Q Surrender of Trust or Investment Management License. Any NBFI which has been authorized to engage in trust and other fiduciary business or in investment management activities and which intends to surrender said authority shall file with the BSP a certified copy of the resolution of its board of directors manifesting such intention. The appropriate department of the SES shall then conduct an examination of the institution's trust, other fiduciary business and investment management activities. If the institution is found to have satisfactorily discharged its duties and responsibilities as trustee, fiduciary or investment manager, and has provided for the orderly closure or transfer of its trust, fiduciary or IMAs, the Monetary Board, on the basis of the recommendation of the examining department, shall order the withdrawal of the institution's authority to engage in trust and other fiduciary management activities.

Secs. 4430Q - 4440Q (Reserved)

Sec. 4441Q Securities Custodianship and Securities Registry Operations. The following rules and regulations shall govern securities custodianship and securities registry operations of QBs/trust entities.

The guidelines to implement the delivery by the seller of securities to the buyer or to his designated third party custodian are shown in *Appendix Q-38*.

Violation of any provision of the guidelines in *Appendix Q-38* shall be subject to the sanctions/penalties under Subsec. 4441Q.29.

(As amended by M-2007-002 dated 23 January 2007, M-2006-009 dated 06 July 2006, M-2006 002 dated 05 June 2006 and Circular No. 524 dated 31 March 2006)

§ 4441Q.1 *Statement of policy*. It is the policy of the BSP to promote the protection of investors in order to gain their confidence and encourage their participation in the development of the domestic capital market. Therefore, the following rules and regulations are promulgated to enhance transparency of securities transactions with the end in view of protecting investors.

§ 4441Q.2 *Applicability of this regulation.* This regulation shall govern securities custodianship and securities registry operations of banks and NBFIs under BSP supervision. It shall cover all their transactions in securities as defined in Section 3 of the SRC, whether exempt or required to be registered with the SEC, that are sold, borrowed, purchased, traded, held under custody or otherwise transacted in the Philippines where at least one (1) of the parties is a bank or an NBFI under BSP supervision. However, this regulation shall not cover the operations of stock and transfer agents duly registered with the SEC pursuant to the provisions of SRC Rule 36-4.1 and whose only function is maintain the stock and transfer book for shares of stock.

§ 4441Q.3 *Prior Bangko Sentral approval.* QBs/trust entities may act as securities custodian and/or registry only upon prior Monetary Board approval.

§ 4441Q.4 *Application for authority* A QB/trust entity desiring to act as securities custodian and/or registry shall file an application with the appropriate department of the SES. The application shall be signed by the highest ranking officer of the institution and shall be accompanied by a certified true copy of the resolution of its board of directors authorizing the institution to engage in securities custodianship and/or registry.

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§ 4441Q.5 ***Pre-qualification requirements for a securities custodian/ registry***

a. It must be a QB or a trust entity;

b. It must have complied with the minimum capital accounts required under existing regulations not lower than an adjusted capital of P300 million or such amounts as may be required by the Monetary Board in the future;

c. It must have a CAMELS composite rating of at least "4" (as rounded off) in the last regular examination;

d. It must have in place a comprehensive risk management system approved by its board of directors appropriate to its operations characterized by a clear delineation of responsibility for risk management, adequate risk

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measurement systems, appropriately structured risk limits, effective internal control and complete, timely and efficient risk reporting systems. In this connection, a manual of operations (which includes custody and/or registry operations) and other related documents embodying the risk management system must be submitted to the appropriate department of the SES at the time of application for authority and within thirty (30) days from updates;

e. It must have adequate technological capabilities and the necessary technical expertise to ensure the protection, safety and integrity of client assets, such as:

(1) It can maintain an electronic registry dedicated to recording of accountabilities to its clients; and

(2) It has an updated and comprehensive computer security system covering system, network and telecommunication facilities that will:

(a) limit access only to authorized users;

(b) preserve data integrity; and

(c) provide for audit trail of transactions.

f. It has complied, during the period immediately preceding the date of application, with the following:

(1) ceilings on credit accommodation to DOSRI; and

(2) single borrower's limit.

g. It has no reserve deficiencies during the eight (8) weeks immediately preceding the date of application;

h. It has set up the prescribed allowances for probable losses, both general and specific, as of date of application;

i. It has not been found engaging in unsafe and unsound practices during the last six (6) months preceding the date of application;

j. It has generally complied with laws, rules and regulations, orders or instructions of the Monetary Board and/or BSP Management;

k. It has submitted additional documents/information which may be requested by the appropriate department of the SES, such as, but not limited to:

(1) Standard custody/registry agreement and other standard documents;

(2) Organizational structure of the custody/registry business;

(3) Transaction flow; and

(4) For those already in the custody or registry business, a historical background for the past three (3) years;

l. It shall be conducted in a separate unit headed by a qualified person with at least two (2) years experience in custody/ registry operations; and

m. It can interface with the clearing and settlement system of any recognized exchange in the country capable of achieving a real time gross settlement of trades.

§ 4441Q.6 *Functions and responsibilities of a securities custodian.* A securities custodian shall have the following basic functions and responsibilities:

a. Safekeeps the securities of the client;

b. Holds title to the securities in a nominee capacity;

c. Executes purchase, sale and other instructions;

d. Performs at least a monthly reconciliation to ensure that all positions are properly recorded and accounted for;

e. Confirms tax withheld;

f. Represents clients in corporate actions in accordance with the direction provided by the securities owner;

g. Conducts mark-to-market valuation and statement rendition;

h. Does earmarking of encumbrances or liens such as, but not limited to, Deeds of Assignment and court orders; and

In addition to the above basic functions, it may perform the following value-added service to clients:

i. Acts as a collecting and paying agent: *Provided*, That the management of funds that may be collected shall be clearly defined in the custody contract or in a separate document or agreement attached thereto: *Provided, further*, That the custodian shall immediately make known to the securities owner all payments made and collections received with respect to the securities under custody;

j. Securities borrowing and lending operations as agent.

§ 4441Q.7 *Functions and responsibilities of a securities registry*

a. Maintains an electronic registry book;

b. Delivers confirmation of transactions and other documents within agreed trading periods;

c. Issues registry confirmations for transfers of ownership as it occurs;

d. Prepares regular statement of securities balances at such frequency as may be required by the owner on record but not less frequent than every quarter; and

e. Follows appropriate legal documentation to govern its relationship with the Issuer.

§ 4441Q.8 *Protection of securities of the customer.* A custodian must incorporate the following procedures in the discharge of its functions in order to protect the securities of the customer:

a. *Accounting and recording for securities*. Custodians must employ accounting and safekeeping procedures that fully protect customer securities. It is essential that custodians segregate customer securities from one another and from its proprietary holdings to protect the same from the claims of its general creditors.

All securities held under custodianship shall be recorded in the books of the custodian at the face value of said securities in a separate subsidiary ledger account *"Securities Held Under Custodianship"* if booked in the Bank Proper or the subsidiary ledger account *"Safekeeping and Custodianship – Securities Held Under Custodianship"*, if booked in the Trust Department: *Provided*, That securities held under custodianship where the custodian also performs securities borrowing and lending as agent shall be booked in the Trust Department.

b. *Documentation*. The appropriate documentation for custodianship shall be made and it shall clearly define, among others, the authority, role, responsibilities, fees and provision for succession in the event the custodian can no longer discharge its functions. It shall be accepted in writing by the counterparties.

The governing custodianship agreement shall be pre-numbered and this number shall be referred to in all amendments and supplements thereto.

c. *Confirmation of custody*. The custodian shall issue a custody confirmation to the purchaser or borrower of securities to evidence receipt or transfer of securities as they occur. It shall contain, as a minimum, the following information on the securities under custody:

(1) Owner of securities;
(2) Issuer;
(3) Securities type;
(4) Identification or serial numbers;
(5) Quantity;
(6) Face value; and
(7) Other information, which may be requested by the parties.

d. *Periodic reporting*. The custodian shall prepare at least quarterly (or as frequent as the owner of securities will require) securities statements delivered to the registered owner's address on record. Said statement shall present detailed information such as, but not limited to, inventory of securities, outstanding balances, and market values.

§ 4441Q.9 ***Independence of the registry and custodian.*** A BSP-accredited securities registry must be a third party with no subsidiary/affiliate relationship with the issuer of securities while a BSP-accredited custodian must be a third party with no subsidiary/affiliate relationship with the issuer or seller of securities. A QB trust entity accredited by BSP as securities custodian may, however, continue holding securities it sold under the following cases:

a. where the purchaser is a related entity acting in its own behalf and not as agent or representative of another;

b. where the purchaser is a non-resident with existing global custody agreement governed by foreign laws and conventions wherein the institution is designated as custodian or sub-custodian; and

c. upon approval by the BSP, where the purchaser is an insurance company whose custody arrangement is either governed by a global custody agreement where the QB/trust entity is designated as custodian or sub-custodian or by a direct custody agreement with features at par with the standards set under this Subsection drawn or prepared by the parent company owning more than fifty percent (50%) of the capital stock of the purchaser and executed by the purchaser itself and its custodian.

Purchases by non-residents and insurance companies that are exempted from the independence requirement of this Section shall, however, be subject to all other provisions of this Subsection.

§ 4441Q.10 ***Registry of scripless securities of the Bureau of the Treasury*** The Registry of Scripless Securities (RoSS), operated by the Bureau of the Treasury, which is acting as a registry for government securities is deemed to be automatically accredited for purposes of this Section and is likewise exempted from the independence requirement under Subsec. 4441Q.9. However, securities registered under the RoSS shall only be considered delivered if said securities were transferred by means of book entry to the appropriate securities account of the purchaser or his designated custodian. Book entry transfer to a sub-account for clients under the primary account of the seller shall not constitute delivery for purposes of this Section and of Subsec. 4235Q.5.

§ 4441Q.11 ***Confidentiality.*** A BSP-accredited securities custodian/registry shall not disclose to any unauthorized person any information relative to the securities under its custodianship/registry. The management shall likewise ensure the confidentiality of client accounts of the custody or registry unit from other units within the same organization.

§ 4441Q.12 ***Compliance with anti-money laundering laws/regulations.*** For purposes of compliance with the requirements of R.A. No. 9160, otherwise known as the "Anti-Money Laundering Act of 2001," as amended, particularly the provisions regarding customer identification, record keeping and reporting of suspicious transactions, a BSP-accredited custodian may rely on referral by the seller/ issuer of securities: *Provided,* That it maintains a record of such referral together with the minimum identification, information/documents required under the law and its implementing rules and regulations.

A BSP accredited custodian must maintain accounts only in the true and full name of the owners of the security. However, said securities owners may be identified by number or code in reports and correspondences to keep his identity confidential.

Securities subject of pledge and/or deed of assignment as of 14 October 2004 (date of Circular 457), may be held by a lending QB up to the original maturity of the loan or full payment thereof, whichever comes earlier.

§ 4441Q.13 *Basic security deposit* Securities held under custodianship whether booked in the Trust Department or carried in the regular books of the QB/trust entity shall be subject to a security deposit for faithful performance of duties at the rate of 1/25 of one percent (1%) of the total face value or P500,000 whichever is higher.

However, securities held under custodianship where the custodian also performs securities borrowing and lending as agent shall be subject to a higher basic security deposit of one percent (1%) of the total face value. For this purpose, the following subsidiary ledger account shall be created in the Trust Department Books:

"Safekeeping and Custodianship - Securities Held Under Custodianship with Securities Borrowing and Lending As Agent"

Compliance shall be in the form of government securities deposited with the BSP eligible pursuant to existing regulations governing security for the faithful performance of trust and other fiduciary business.

§ 4441Q.14 *Reportorial requirements* An accredited securities custodian shall comply with reportorial requirements that may be prescribed by the BSP, which shall include as a minimum, the face and market value of securities held under custodianship.

§§ 4441Q.15 - 4441Q.28 *(Reserved)*

§ 4441Q.29 *Sanctions.* Without prejudice to the penal and administrative sanctions provided for under Sections 36 and 37, respectively, of the R.A. No. 7653, violation of any provision of this Section shall be subject to the following sanctions/ penalties:

a. *First offense* –

(1) Fine of up to P10,000 a day for the institution for each violation reckoned from the date the violation was committed up to the date it was corrected; and

(2) Reprimand for the directors/officers responsible for the violation.

b. *Second offense* -

(1) Fine of up to P20,000 a day for the institution for each violation reckoned from the date the violation was committed up to the date it was corrected; and

(2) Suspension for ninety (90) days without pay of directors/officers responsible for the violation.

c. *Subsequent offenses* –

(1) Fine of up to P30,000 a day for the institution for each violation from the date the violation was committed up to the date it was corrected;

(2) Suspension or revocation of the authority to act as securities custodian and/or registry; and

(3) Suspension for 120 days without pay of the directors/officers responsible for the violation.

Secs. 4442Q - 4498Q (Reserved)

Sec. 4499Q Sanctions. Any violation of the provisions of this Part shall be subject to Sections 36 and 37 of R.A. No. 7653, without prejudice to the imposition of other sanctions as the Monetary Board may consider warranted under the circumstances that may include the suspension or revocation of an institution's authority to engage in trust and other fiduciary business or in investment management activities, and such other sanctions as may be provided by law.

The guidelines for the imposition of monetary penalty for violations/offenses with sanctions falling under Section 37 of R. A. No. 7653 on QBs, their directors and/or officers are shown in *Appendix Q-39*.

PART FIVE

FOREIGN EXCHANGE OPERATIONS

Section 4501Q Authority; Coverage With prior approval of the Monetary Board, and subject to the provisions of Article III, Chapter IV of R.A. No. 7653 and Section 7(13) of P.D. No. 129, as amended, an IH may engage in foreign exchange operations which shall be limited to the servicing of project or program requirements of the following enterprises:

a. BSP-certified export-oriented firms;

b. Board of Investments-registered export-oriented firms; and

c. Construction or service firms with overseas contracts approved by the Department of Labor and Employment.

Sec. 4502Q Specific Foreign Exchange Activities. The specific foreign exchange operations which IHs may undertake in connection with the preceding Section are:

a. Arranging or contracting of foreign loans for the account of the client firm, or contracting of foreign loans for the account of the IH for relending to the client firm, subject to pertinent BSP rules and regulations;

b. Providing import- and export-related services to said firms such as letters of credit and other acceptable modes of payment, and the discounting of export drafts: *Provided,* That the total amount of foreign exchange transactions IHs may deal in shall not exceed the amount of the financing arranged or provided by the IH which involves the importation and exportation of related goods and services: *Provided, further,* That the amount of letters of credit outstanding of an IH shall not exceed, at any given time, twice its net worth, except as may otherwise be specifically authorized by the Monetary Board;

c. Holding foreign currency balances with foreign correspondents in connection with export-related services but in no case for speculative purposes;

d. Entering into forward foreign exchange contracts with the BSP in connection with the foregoing activities; and/or

e. Such other related foreign exchange activities as may be approved by the Monetary Board.

Sec. 4503Q Separate Department. Any IH that may be authorized to engage in foreign exchange operations shall set up a separate department/unit to handle such operations.

Sec. 4504Q Applicability of Pertinent Bangko Sentral Rules. The foreign exchange operations of an IH are subject to all applicable BSP rules and regulations on foreign exchange operations, including modifications thereof, considering the special nature of IH operations, and the sanctions in connection therewith.

Sec. 4505Q Aggregate Ceiling on Issuance of Guarantees. Total standby letters of credit, foreign and domestic, including guarantees, the nature of which requires the guarantor to assume the liabilities/obligations of third parties in case of their inability to pay, that may be issued by QBs and outstanding at any given time, shall not exceed fifty percent (50%) of the QB's net worth, except those fully secured by cash, hold-out on deposits/ deposit substitutes on government securities.

Secs. 4506Q - 4598Q (Reserved)

Sec. 4599Q General Provision on Sanctions. Any violation of the provisions of this Part shall be subject to Sections 36 and 37 of R.A. No. 7653.

The guidelines for the imposition of monetary penalty for violations/offenses with sanctions falling under Section 37 of R.A. No. 7653 on QBs, their directors and/or officers are shown in *Appendix Q-39*.

PART SIX

TREASURY AND MONEY MARKET OPERATIONS

A. OPEN MARKET OPERATIONS

Section 4601Q Open Market Operations The following rules and regulations shall govern the buying and selling of government securities in the open market pursuant to Section 91 of R.A. No. 7653:

a. The BSP may buy and sell in the open market for its own account:

(1) Evidences of indebtedness issued directly by the Government of the Philippines or by its political subdivisions; and

(2) Evidences of indebtedness issued by government instrumentalities and fully guaranteed by the Government.

The above evidences of indebtedness must be freely negotiable and regularly serviced and must be available to the general public through banks, QBs and accredited government securities dealers.

b. Outright purchases and sales of government securities shall be effected on the basis of the lowest price offered or the highest price bid.

c. Repo agreements shall be open to banks (except RBs), QBs and accredited government securities dealers and shall be made under the terms provided for in Sec. 4601Q.1 and the following:

(1) The repo agreement may be paid at any time before maturity at the option of the issuer of the repo agreement;

(2) In the event the securities covered by the repo agreement are not repurchased by the issuer of such agreement, they may be sold in the open market or transferred to the BSP Portfolio; and

(3) Should an issuer of a repo agreement become no longer qualified as such, its outstanding repo agreement shall immediately become due and payable. If settlement of the amount due is not made within three (3) days from the date of its disqualification, the BSP shall proceed to collect said amount in accordance with the preceding paragraph.

d. Reverse repo agreements covering the sale of portion of the security holdings of the BSP portfolio may be made under the terms provided for in Subsec. 4601Q.2.

§ 4601Q.1 ***(2008 - 4602Q) Repurchase agreements with the Bangko Sentral.*** Repo agreements may be effected with the BSP subject to the following terms and conditions:

a. *Rate*. The rates on the repurchase facility shall be set by the Treasury Department, with the concurrence of the Governor, taking into account prevailing liquidity/market conditions.

b. *Term*. At the option of the Treasury Department, availments may be for a minimum of one (1) day (overnight) and a maximum of ninety-one (91) days.

c. *Security*. Only obligations of the National Government and its instrumentalities and political subdivisions, which are fully guaranteed by the Government, with a remaining maturity of not more than ten (10) years and which are freely negotiable and regularly serviced, shall be eligible as underlying instruments for repo agreements, subject to the collateral requirement prescribed by the BSP.

d. *Delivery*. Delivery of the underlying instruments shall be made to the BSP at the prescribed time. For overnight repo agreements, delivery of the underlying instruments shall be made not later than 12:00 noon of the date of transaction.

Government securities which are held by the issuer of the repo agreement under the book-entry system with the BSP may be used as underlying instruments only with the conformity of the BSP.

e. Upon termination of the repo agreement, the issuer of such agreement shall claim and take delivery of the underlying instruments at the Treasury Department, BSP. Failure to claim and take delivery of the underlying instruments immediately upon such termination shall relieve the BSP of any liability or responsibility for the loss or misplacement of said instruments.

§ 4601Q.2 ***(2008 - 4602Q.1) Reverse repurchase agreements with Bangko Sentral.*** Reverse repo agreements may be effected with the BSP subject to the following terms and conditions:

a. *Rate*. The rates shall be set by the Treasury Department, with the concurrence of the Governor, taking into account the prevailing liquidity/market conditions.

b. *Term*. At the option of the Treasury Department, availments may be for a minimum of one (1) day (overnight) and a maximum of 364 days.

c. *Security*. The collateral shall consist of obligations of the National Government and other freely negotiable securities in the BSP portfolio valued at 100%.

d. *Delivery*. No delivery of the collateral shall be made, but a custody receipt shall be issued instead.

e. *Reservation*. Prepayment may be made by the BSP at its option anytime before maturity.

Effective 01 July 2003, published interest rates that will be applied on BSP's reverse repo agreements shall be inclusive of Value Added Tax (VAT).

Reverse repo agreements entered into by the BSP with any authorized agent bank (AAB) are included in the definition of the term "*deposit substitutes*" under Sec. 22 (y) Chapter 1 of the National Internal Revenue Code of 1997.

The BSP shall withhold twenty percent (20%) Final Withholding Tax (FWT) on its overnight reverse repo agreements starting January 01, 2008, under the following guidelines:

(1) All overnight reverse repo agreements with the BSP shall be subject to the twenty percent (20%) FWT in the same manner as term reverse repo agreements, which tax is deducted on each maturity date and remitted to the BIR;

(2) With respect to the overnight RRPs from 01 January 2008 to 22 August 2008[1], the concerned QBs shall reimburse the BSP the amount equivalent to forty percent (40%) of the twenty percent (20%) FWT due thereon. However, QBs which choose to pay the whole twenty percent (20%) FWT shall remit the amount equivalent to the sixty percent (60%) balance thereof to the BIR, through the BSP as withholding agent. In both cases, payment of the FWT to the BSP shall be made on or before 03 April 2009, either in full or in three (3) installments: *Provided*, That a QB which intends to pay in installments shall remit the first payment on or before 06 March 2009, the second on or before 20 March 2009 and the last on or before 03 April 2009: *Provided, further,* That payments due shall be deducted from the Regular Demand Deposit Account (RDDA) of concerned QBs. The BSP shall issue the certificate of final withholding tax reflecting the amount of the FWT paid; and

(3) Concerned banks shall issue the corresponding debit authority to the BSP to cover the twenty percent (20%) FWT on their overnight reverse repo agreements with the BSP mentioned in Item "*2*" above.

(As amended by Circular Nos. 647 dated 03 March 2009, 636 dated 17 December 2008 and 619 dated 22 August 2008)

[1] Interest income payments from 01 January 2008 to 26 August 2008.

§ 4601Q.3 ***(2008 - 4601Q.1) Settlement procedures.*** Purchase and sale of government securities under repo agreements (GS/repo agreements) between and among banks and QBs and BSP in connection with the latter's open market operations shall be settled in accordance with the provisions of the agreement for the PhilPaSS executed on 12 December 2002 between the BSP and IHAP and any subsequent amendments thereto.

(As superseded by the agreement between the BSP and IHAP dated 12 December 2002)

§§ 4601Q.4 - 4601Q.5 ***(Reserved)***

§ 4601Q.6 ***Bangko Sentral trading windows and services during public sector holidays.*** The guidelines on BSP's trading windows and services during public sector holidays are shown in *Appendix Q-49*.

(M-2008-025 dated 13 August 2008)

Secs. 4602Q - 4610Q ***(Reserved)***

B. FINANCIAL INSTRUMENTS

Sec. 4611Q ***(2008 - 4603Q)*** **Derivatives**. A QB may engage in authorized derivatives activities: *Provided,* That a QB:

a. Understands, measures, monitors and controls the risks assumed from its derivatives activities;

b. Adopts effective risks management practices whose sophistication are commensurate to the risks being monitored and controlled; and

c. Maintains capital commensurate with the risk exposures assumed.

Further, a QB may engage in financial derivatives activities in accordance with these guidelines. The transacting QB shall have the responsibility to comply with the guidelines set out in this Section, including the relevant appendices, and other applicable laws, rules and regulations governing derivatives transactions. In case of derivatives instruments involving foreign currencies and/or other foreign currency-denominated assets, the transacting QB shall observe the pertinent foreign exchange ("FX") rules and regulations. For purposes of these guidelines, a QB that transacts (i.e., transacting bank), whether as end-user, broker or dealer, in derivatives instruments is considered to be engaging in a derivatives activity.

Derivative is broadly defined as a financial instrument that primarily derives its value from the performance of an underlying variable. For purposes of these guidelines, a *financial derivative* is any financial instrument or contract with all of the following characteristics:

a. Its value changes in response to a change in a specified interest rate, financial instrument price, commodity price, FX rate, index of prices or rates, credit spread, credit rating or credit index or other variables not prohibited under existing laws, rules and regulations ("the underlying");

b. It requires either no initial net investment or an initial net investment that is smaller than would be required for other types of contracts that would be expected to have a similar response to changes in market factors; and

c. It is settled at a future date.

Financial derivatives activities shall also include transactions in cash instruments with embedded derivatives that reshape the risk-return profile of the host instrument, such as credit-linked notes ("CLNs") and their structured products ("SPs").

A market participant may take any of the following roles in a derivatives transaction:

a. An *end-user* is defined as a financial market participant that enters, for its own account, in a derivatives transaction for legitimate economic purposes. These purposes may include, but are not limited

to, the following: hedging proprietary trading, managing capital or funding costs, obtaining indirect exposures to desired market factors, investment, yield-enhancement, and/or altering the risk-reward profile of a particular item or an entire balance sheet.

An end-user may be classified according to its financial sophistication:

(1) *Market counterparty* - refers to FI, only with respect to the instruments for which it is authorized to engage in as a dealer;

(2) *Institutional counterparty* - refers to an institution which is not a market counterparty and has the level of net worth, knowledge, expertise, and experience to deal with financial derivatives;

(3) *Sophisticated individual end-user* - refers to an individual who has demonstrated to the FI as having the level of net worth, knowledge and experience in dealing with financial products, including financial derivatives. An individual may register as a sophisticated individual end-user with the Centralized Applications and Licensing Group of the BSP.

(4) *Other end-user* - this refers to all other institutional or individual clients not categorized as market counterparty, institutional counterparty or sophisticated individual end-user.

b. A *broker* is a financial market participant that facilitates a derivatives transaction between a dealer and its client, for a fee or commission. The counterparties to the derivatives contract are the client and an authorized dealer.

c. A *dealer* is defined as a financial market participant that engages in a derivatives activity as an originator of derivatives products or as market-maker in derivatives products. A dealer can distribute its own derivatives products, including those of others. A dealer can also act as broker and/or end-user of derivatives instruments.

(As amended by Circular No. 668 dated 02 October 2009)

§ 4611Q.1 ***(2008 - 4603.Q.1) Generally authorized derivatives activities.*** A QB may enter in any financial derivatives transaction with BSP-authorized dealers and brokers without need of prior BSP approval solely for hedging purposes: *Provided,* That it observes all the requirements for hedging transactions under Philippines Accounting Standards ("PAS"): *Provided further*, That it observes the provisions of *Appendix Q-15*.

A trust department of a QB may enter, as an institutional counterparty, into any financial derivatives with the BSP-approved authorized dealers and brokers, on behalf of its trustor/principal/s as may be authorized by such trustor/principals/s without need of prior BSP approval, solely for hedging purposes: *Provided*, That the trust department observes all the requirements for hedging transactions under PAS: *Provided further*, That it observes the provisions of *Appendix Q-15*.

(As amended by Circular No. 668 dated 02 October 2009)

§ 4611Q.2 ***(2008 - 4603Q.2) Activities requiring additional derivatives authority*** QB may apply for prior BSP approval of additional derivatives authority to engage in all other financial derivatives activities not expressly allowed in Subsec. 4611Q.1. A QB may apply for two (2) or more additional authorities. A QB applying for additional derivatives authority/ies must have and maintain a risk management system commensurate to the additional authority/ies being applied for, in accordance with the provisions of *Appendix Q-15* and meet other conditions specified under this Subsection.

a. *Classification of additional derivatives authority*

(1) Type 2 - Limited Dealer Authority

A QB that is also an investment house may apply for a Type 2 Authority. A QB with Type 2 Authority may operate as a dealer in specific types of derivatives products with specific underlying reference,

as applied for by the QB: *Provided*, That a QB with Type 2 Authority shall comply with the sales and marketing guidelines prescribed in *Appendix Q-16*. The Type 2 Authority also carries authority to transact as broker and end-user of the said specific derivatives instruments.

(2) Type 3 - Limited User Authority

A QB or a trust department of a QB, may apply for a Type 3 Authority. A QB or a trust department of a QB with Type 3 Authority may transact, as an end-user, in specific types of derivatives product, with specific underlying reference, as applied for by the QB, outside of those instruments that meet the conditions under Subsec. 4611Q.1. A Type 3 Authority will enable said QB or trust department to transact as end-user of derivatives instruments as may be applied for by the QB or trust department.

(3) Type 4 - Special Broker Authority

A QB that is also an investment house may likewise apply for a Type 4 Authority. A QB with Type 4 Authority may facilitate a derivatives transaction between a BSP-authorized dealer and end-user clients: *Provided,* That the QB, acting as broker, ensures that its client fully understands its limited responsibility as a broker and observes the provisions of *Appendix Q-16*.

A QB with additional Type 2 or 4 Authorities shall be responsible for complying with pertinent securities laws, rules and regulations.

For purposes of this Subsection, the types of derivatives are classified as follows: forwards, swaps and options. *Underlying reference* pertains to the following: interest, foreign currencies/ foreign exchange, equity, credit and commodity.

b. *Qualification requirements*. A QB applying for additional authority to engage in additional derivatives activities shall:

(1) Demonstrate adequate competence in its general operations as evidenced by:

(a) CAMELS composite rating of at least *"3"* with a similar rating for Management, as applicable;

(b) No unresolved major safety and soundness issues that threaten liquidity or solvency; and

(c) Substantial compliance with regulations on anti-money laundering, corporate governance and risk management.

(2) Hold capital commensurate to the risks assumed or to be assumed from the derivatives activities. A QB applying for or holding a Type 2 Limited Dealer Authority or Type 3 Limited User Authority automatically agrees to be covered by all regulations prescribing capital for market risk, notwithstanding any provision to the contrary. In addition, the BSP expects a QB applying for or holding additional derivatives authority to have adequate capital to accommodate existing and future risks from additional and generally authorized derivatives activities as well as risks arising from the QB's other business activities. For this purpose, the BSP may require capital higher than the minimum required under prudential regulations.

(3) Have and maintain a risk management system that conforms to the principles and complies with the minimum standards prescribed in *Appendix Q-15*.

(4) Demonstrate the relevance of proposed derivatives activities to the QB's main purpose as an institution. The BSP reserves the right to deny applications whose proposed derivatives activities do not reasonably fit the nature of their business operations.

c. *Applicability to trust department of QBs*. Trust departments of QBs may apply for Type 3 Authority, provided they comply with the requirements prescribed and observe the provisions of *Appendix Q-15 and Q-16*.

d. *Application procedures*. The applicant shall submit to the Capital Markets Specialist Group, SES of the BSP a written

application for additional derivatives authority/ies accompanied by;

(1) A copy of the board resolution approving the application for a specific type of derivatives authority;

(2) A notarized certification signed jointly by the president, treasurer, or equivalent trust officer and compliance officer of the applicant QB stating that the QB complies with all the requirements for the authority being applied for specified in Subsec. 4611Q.2; and

(3) A list of the types of derivatives and underlying reference the QB intends to engage in, including the following information for each derivatives class or type:

(a) Target customers for such derivatives;

(b) The capacity in which the QB intends to engage in such derivatives;

(c) Description of each type of derivatives and underlying reference with which it will deal;

(d) Analysis of the risks involved in transacting in each type of derivatives;

(e) Procedures/methodologies that the QB will implement to measure, monitor (including risk management reports) and control the risks inherent in the type of derivatives;

(f) Relevant accounting guidelines, including pro-forma accounting entries;

(g) Analysis of any actual or potential legal/regulatory restrictions; and

(h) Process flow chart, from deal initiation to risk reporting, indicating the departments and personnel involved in identified processes.

(4) The BSP will not accept applications lacking any of the above-stated requirements. The BSP, however, may require additional documents to aid its evaluation of the application. By virtue of the application, the applicant automatically authorizes the BSP to conduct an on-site evaluation of the applicant's risk management capabilities, if this is deemed necessary.

(5) Payment of the following non-refundable processing fee shall be made upon approval or denial of the QB's application:

	Amount
Type 2 Authority	P 50,000.00
Type 3 Authority	25,000.00
Type 4 Authority	25,000.00

(6) A QB whose application for additional derivatives authority/ies or an upgrade thereof (e.g., from Type 3 to Type 2 Authority) has been denied cannot submit a new application for additional derivatives authorities until after six (6) months from receipt of denial. The same rule applies for a QB whose authorities have been limited or downgraded.

(7) A QB that holds an additional derivatives authority may apply for additional derivatives authorities (e.g., currently holding Type 3 Authority who wish to apply for Type 4 Authority) or an upgrade thereof only after the lapse of six (6) months from the grant of the previous additional derivatives authority.

(As amended by Circular No. 668 dated 02 October 2009)

§ 4611Q.3 ***(2008 - 4603Q.3) Intra-group transactions.*** All derivatives transactions between a QB and any of its subsidiaries and affiliates shall comply with minimum risk management standards for related-party transactions outlined in *Appendix Q-15* as part of the QB's internal control procedures. The BSP expects QBs to establish internal reporting and monitoring system for derivatives activities for related-party transactions. Failure to comply with minimum standards shall be a ground for citing non-compliance with provisions under Subsecs. 4611Q.1 and 4611Q.2 without prejudice to other BSP rules and regulations such as those related

to corporate governance and unsafe and unsound banking practices.
(As amended by Circular No. 668 dated 02 October 2009)

§ 4611Q.4 ***(2008 - 4603Q.5) Accounting guidelines.*** A QB that engages in derivatives activities must strictly account for such transactions in accordance with relevant PAS.
(As amended by Circular No. 668 dated 02 October 2009)

§ 4611Q.5 ***(2008 - 4603Q.6) Reporting requirements.*** A QB engaged in any derivatives transactions shall submit a monthly report on derivatives transactions/ outstanding derivatives in accordance with the format shown in Annex *"A"* of *Appendix Q-16* within fifteen (15) banking days from end of the reference month. The reports shall be certified by the treasurer.
(As amended by Circular No. 668 dated 02 October 2009)

§ 4611Q.6 ***(2008 - 4603Q.7) Sanctions***

a. *Unauthorized transactions*

Sanctions prescribed under Sections 36 and 37 of R.A. No. 7653 shall be imposed on any QB (including its directors and officers) found to have engaged in an unauthorized derivatives activity.

A QB undertaking unauthorized derivatives activities may be considered as conducting its business in an unsafe and unsound manner under Section 56 of R.A. No. 8791.

b. *Delayed/Erroneous/Inaccurate reporting*

QBs failing to submit the reports required under Subsec. 4611Q.5 within the prescribed deadline shall be subject to monetary penalties applicable for delayed reporting under existing regulations. Moreover, submission of incomplete, uncertified or improperly certified or otherwise erroneous reports shall be considered non-reporting, subject to applicable penalties for amended/delayed reports. For purposes of imposing monetary penalties, the reports shall be classified as a *Category A-1* report. Habitual delayed or erroneous reporting may be a ground for further sanction, including limitation of generally authorized activities and/or additional authorities and/or suspension of authority to engage in such derivatives activities.

c. *Non-compliance with the provisions of this Section, its Subsecsections and Appendices Q-15 and Q-16.*

Any QB found violating any of the provision of Sec. 4111Q and its Subsections and/or *Appendices Q-15* and *Q-16* shall be sanctioned with the penalties prescribed under Sections 36 and 37 of R.A. No. 7653 in accordance with the gravity/seriousness of the offense taking into consideration the number of times the offense was committed, possible consequent losses on the clients, effect on the financial markets and other relevant factors.

d. *Curtailment of derivatives authority*

The BSP reserves the right to suspend, modify, downgrade, limit or revoke any QB's derivatives authority (including any or all of those generally authorized activities) for prudential reasons as may be evidenced by any or all of the following:

i. The QB is assigned a CAMELS composite rating or component Management rating of lower than that prescribed under Subsec. 4611Q.2 in the most recent regular examination.

ii. The QB has not maintained adequate risk management systems given the level and type of derivatives activities it has engaged in as may be determined by the BSP in any on-site evaluation and confirmed by the Monetary Board.

iii. The Monetary Board has confirmed an SES finding that the QB has conducted business in an unsafe and unsound manner.

An erring QB may apply for reinstatement of its derivatives authority

only after six (6) months from lapse of the implementation of the sanction, provided the QB has satisfactorily addressed all the BSP concerns.

(As amended by Circular No. 668 dated 02 October 2009)

Secs. 4612Q - 4624Q (Reserved)

Sec. 4625Q *(2008 - 4603Q.14)* Forward and Swap Transactions

Statement of policy. It is the policy of the BSP to support the deepening of the Philippine financial markets. In line with this policy, customers may, thru FX forwards, hedge their market risks arising from FX obligations and/or exposures: *Provided,* That forward sale of FX (deliverable and non-deliverable) may only be used when the underlying transaction is eligible for servicing by the banking system under FX Manual, as amended. Customers may, likewise, cover their funding requirements thru FX swaps.

QBs may only engage in FX forwards and swap transactions with customers if the latter is hedging market risk or covering funding requirements. There shall be no double/multiple hedging such that at any given point in time, the total notional amount of the FX derivatives transaction/s shall not exceed the amount of the underlying FX obligation/exposure.

The customer shall no longer be allowed to buy FX from the banking system for FX obligations/exposures that are fully covered by deliverable FX forwards and FX swaps.

The following guidelines, as well as minimum documentary requirements, shall cover FX forward and swap transactions involving the Philippine peso between authorized dealer QBs and their customers.

(As amended by Circular No. 591 dated 27 December 2007)

§ 4625Q.1 *(Reserved)*

§ 4625Q.2 *(2008 - 4603Q.15) Definition of terms*

a. *Customers* shall refer to:

(1) resident banks (other than KBs and UBs) and non-bank BSP-supervised entities (NBBSEs) not authorized to engage in FX forwards and swaps as dealers;

(2) resident non-bank entities; and

(3) non-residents, both banks and non-banks.

b. *Foreign exchange obligation* shall refer to an actual commitment to repatriate or pay to a non-resident or any AAB a specific amount of foreign currency on a pre-agreed date.

c. *Foreign exchange exposure* shall refer to an FX risk arising from an existing commitment which will lead to an actual payment of FX to, or receipt of FX assets from, non-residents or any AAB based on verifiable documents on deal date. FX risks arising from BSP-registered foreign investments without specific repatriation dates are considered FX exposures.

d. *Resident* shall refer to -

(1) An individual citizen of the Philippines residing therein; or

(2) An individual who is not a citizen of the Philippines but is permanently residing therein; or

(3) A corporation or other juridical person organized under the laws of the Philippines; or

(4) A branch, subsidiary, affiliate, extension office or any other unit of corporations or juridical persons which are organized under the laws of any country and operating in the Philippines, except offshore banking units (OBUs).

e. *Non-resident* shall refer to an individual, a corporation or other juridical person not included in the definition of resident.

f. *Foreign exchange swap* shall refer to a transaction involving the actual exchange of two (2) currencies (principal amount only) on a specific date at a rate

agreed on deal date (the first leg), and a reverse exchange of the same two (2) currencies at a date further in the future (the second leg) at a rate (different from the rate applied to the first leg) agreed on deal date.

g. *Foreign exchange forward* shall refer to a contract to purchase/sell a specified amount of currency against another at a specified exchange rate for delivery at a specified future date three (3) or more business days after deal date.

h. *Non-deliverable forward (NDF)* shall refer to an FX forward contract where only the net difference between the contracted forward rate and the market rate at maturity (i.e., the fixing rate) shall be settled on the forward date.

(As amended by Circular No. 591 dated 27 December 2007)

§ 4625Q.3 ***(2008 - 4603Q.16) Documentation.*** Minimum documentary requirements for FX forward and swap transactions in *Appendix Q-29* shall be presented on or before deal date to the QBs unless otherwise indicated.

FX selling QBs shall stamp the supporting documents upon presentation by customers as follows:

a. For hedging transactions: *"FX HEDGED/DELIVERABLE"* or *"FX HEDGED/ NON-DELIVERABLE";*

b. For funding transactions: *"FX SOLD",* indicating the contract date and amount involved, and signed by the QB's authorized officer. Copies of all duly marked supporting documents shall be retained by the QBs and made available to the BSP for verification. The retained copies shall also be marked *"DOCUMENTS PRESENTED AS REQUIRED"* and signed by the QB's authorized officer.

(As amended by Circular No. 591 dated 27 December 2007)

§ 4625Q.4 ***(2008 - 4603Q.17) Tenor/ maturity and settlement***

a. *Forward sale of FX (whether deliverable or non-deliverable).* The tenor/ maturity of such contracts shall not be longer than: (i) the maturity of the underlying FX obligation; or (ii) the approximate due date or settlement of the FX exposure. For deliverable FX forward contracts, the tenor/maturity shall be co-terminus with the maturity of the underlying obligation or the approximate due date or settlement of the FX exposure. This shall not preclude pre-termination of the contract due to prepayment of the underlying obligation or exposure: *Provided,* That for foreign currency loans, prior BSP approval has been obtained for the prepayment and a copy of such approval is presented to the QB counterparty.

b. *FX Swaps* - No restriction on tenor.

c. *Settlement of NDFs* - All NDF contracts with residents shall be settled in pesos.

d. *Remittance of FX proceeds of deliverable forward and swap contracts.*

FX proceeds of deliverable forward and swap contracts shall be delivered by the QB counterparty directly to the beneficiaries concerned except for foreign investments where said FX proceeds are reconverted to Philippine pesos and re-invested in eligible peso instruments such as those listed in Item "A.2.2" of *Appendix Q-29*. For this purpose, beneficiaries shall refer to the FCDU of a QB or a non-resident entity (e.g., creditor, supplier, investor) to whom the customer is committed to pay/remit FX.

(As amended by Circular No. 591 dated 27 December 2007)

(Next page is Part VI - Page 7)

§ 4625Q.5 ***(Reserved)***

§ 4625Q.6 ***(2008 - 4603Q.18) Cancellations, roll overs or non-delivery of FX forward and swap contracts.*** All cancellations, roll-overs or non-delivery of all FX deliverable forward contracts and the forward leg of swap contracts shall be subject to the following guidelines to determine the validity thereof:

a. *Eligibility test* - Contracts must be supported by documents listed in *Appendix Q-29* hereof.

b. *Frequency test* - the reasonableness of the cancellation, roll-over or non-delivery shall be based on the results of the evaluation of the justification/explanation submitted by QBs as evidenced by appropriate documents.

c. *Counterparty test* – the cancellation or roll-over of contracts must be duly acknowledged by the counterparty to the contract as shown in documents submitted by QBs, e.g., there should be *conforme* of counterparty as evidenced by the counterparty signature on pertinent documents.

d. *Mark-to-Market test*– the booking or recording in the books of accounts of the profit or loss on contracts and cash flows/settlement to counterparties must be fully supported by appropriate documents such as authenticated copy of debit/credit tickets, schedules showing among others, mark-to-market valuation computation, etc.

(As amended by Circular No. 591 dated 27 December 2007)

§ 4625Q.7 ***(2008 - 4603Q.19) Non-deliverable forward contracts with non-residents.*** Only banks with expanded derivatives license may enter into NDF contracts to sell FX to non-residents.

§ 4625Q.8 ***(2008 - 4603Q.20) Compliance with Anti-Money Laundering rules.*** All transactions under Section 4625Q and Subsecs. 4625Q.2 to 4626Q.4 and 4625Q.6 to 4625Q.9 shall comply with existing regulations on anti-money laundering under Sec. 4801Q.

(As amended by Circular No. 591 dated 27 December 2007)

§ 4625Q.9 ***(2008 - 4603Q.21) Reporting requirements.*** QBs duly authorized to engage in derivatives transactions shall continue to be covered by the BSP's existing reporting requirements on financial derivatives. Cancellations, roll-overs or non-delivery of deliverable FX forward contracts and under the forward leg of swap contracts shall be reported electronically in excel format to the BSP not later than five (5) business days after reference month as indicated in *Appendix Q-3*.

Swap contracts with counterparties involving purchase of FX by QBs at the initial leg shall likewise be reported electronically in excel format to the BSP not later than five (5) business days after reference month as indicated in *Appendix Q-3*.

The reports shall be transmitted to the International Department at iod@bsp.gov.ph, copy furnished the SDC.

(As amended by Circular No. 591 dated 27 December 2007)

§§ 4625Q.10 - 4625Q.13 ***(Reserved)***

§ 4625Q.14 ***(2008 - 4603.26) Sanctions*** Violations of 4625Q and Subsecs. 4625Q.2 to 4626Q.4 and 4625Q.6 to 4625Q.9 shall be subject to the penalty provisions under R.A. No. 7653 (The New Central Bank Act) and other existing banking laws and regulations.

a. Monetary Penalties

Per Calendar Month	Daily Penalty
1st business day	₱ 10,000
2nd business day	20,000
3rd business day of violation, and onwards, or if the excess FX position is 30% or more of the allowable limits in any business day, regardless of whether a QB is in the first, second, third or more days of violation	30,000

b. In addition, the following non-monetary sanctions shall be imposed on the QB committing violations considered as:

(1) *chronic,* i.e., when the violation continues beyond three (3) business days within a calendar month, but the excess position is less than thirty percent (30%) of the allowable limit; and

(2) *abusive*, i.e., when the violation continues beyond three (3) business days within a calendar month and excess position is thirty percent (30%) or more of the allowable limit.

"Chronic" violation	Suspension of the QB's cash dividend declaration and branching privileges until the violation is corrected but in no case shall such suspension be less than thirty (30) calendar days.
" Abusive" violation	Suspension of the QB's cash dividend declaration and branching privileges until the violation is corrected but in no case shall such suspension be less than sixty (60) calendar days.

c. The Monetary Board may impose other non-monetary sanctions on a QB for violations determined by BSP as "chronic" or "abusive" on a case-to-case basis, pursuant to Section 37 of R.A. No. 7653.

d. QBs shall be duly advised by the BSP of their violations and the corresponding sanctions imposed for such violations.

e. A monetary penalty imposed on a QB shall be paid to the BSP Cash Department, within three (3) business days from the receipt of advice of said penalty imposition.

For purposes of imposing sanctions for delayed, erroneous or unsubmitted reports, reports required under Subsec. 4625Q.9 are classified as *Category B* reports and subject to corresponding penalties.

Counterparties that habitually cancel deliverable forwards without proper justification may be subject of a BSP watchlist.

(As amended by Circular No. 591 dated 27 December 2007)

Secs. 4626Q - 4650Q *(*Reserved*)*

Sec. 4651Q *(2008 - 4626Q)* Asset-Backed Securities. The following regulations shall govern the origination, issuance, sale, servicing and administration of asset-backed securities (ABS) by any QB including its subsidiaries and affiliates engaged in allied activities, which are domiciled in the Philippines.

§ 4651Q.1 *(2008 - 4626Q.1) Definition of terms*

a. *Assets* shall mean loans or receivables existing in the books of the originator prior to securitization. Such assets are generated in the ordinary course of business of the originator and may include mortgage loans, consumption loans, trade receivables, lease receivables, credit card receivables and other similar financial assets.

b. *Asset-backed securities* shall refer to the certificates issued by a special purpose trust (SPT) representing undivided ownership interest in the asset pool.

c. *Asset pool* shall mean a group of identified, self-amortizing assets that is conveyed to the SPT issuing the ABS and such other assets acquired as a consequence of the securitization.

d. *Clean-up call* shall refer to an option granted to the seller to purchase the remaining assets in the asset pool.

e. *Credit enhancement* shall refer to any legally enforceable scheme that is intended to enhance the marketability of the ABS and increase the probability that investors receive payment of amounts due them.

f. *Guarantor* shall refer to an entity that guarantees the repayment of principal and interests on loans or receivables included in the asset pool in the event of default by the borrower.

g. *Investible funds* shall refer to the proceeds of collection of loans or receivables included in the asset pool which are not yet due for distribution to investors.

h. *Issuer* shall refer to the SPT that issues the ABS.

i. *Originator* shall refer to a QB and/or its subsidiary or affiliate engaged in allied activities that grants or purchases loans or receivables and assembles them into a pool for securitization.

j. *Residual certificates* shall refer to certificates issued representing claims on the remaining value of the asset pool after all ABS holders are paid.

k. *Seller* shall refer to the entity which conveys to the SPT the assets that constitute the asset pool.

l. *Servicer* shall refer to the entity designated by the issuer primarily to collect and record payments received on the assets, to remit such collections to the issuer and perform such other services as may be specifically required by the issuer excluding asset management or administration.

m. *Special purpose trust* shall refer to a trust administered by a trustee and created solely for the purpose of issuing and administering an ABS.

n. *Trustee* shall refer to the entity designated to administer the SPT.

o. *Underwriter* shall refer to the entity engaged in the act or process of distributing and selling of the ABS either on guaranteed or best-efforts basis.

§ 4651Q.2 ***(2008 - 4626Q.2) Authority*** Any QB including its subsidiaries and affiliates engaged in allied activities, may securitize its assets upon prior approval of the BSP.

§ 4651Q.3 ***(2008 - 4626Q.3) Management oversight.*** The originator/seller shall have the securitization program approved by its board of directors. The originator/seller shall integrate such securitization program into its corporate strategic plan. The board of directors shall ensure that the securitization of assets is consistent with such program.

§ 4651Q.4 ***(2008 - 4626Q.4) Minimum documents required.*** The application to securitize must be accompanied by the following documents as a minimum requirement:

a. *Trust indenture* evidencing the conveyance of the assets from the seller to the issuer or SPT, the features of which shall include the following:

(1) Title or nature of the contract in noticeable print;

(2) The parties involved, indicating in noticeable print, their respective legal capacities, responsibilities and functions;

(3) Features and amount of ABS;

(4) Purposes and objectives;

(5) Description and amount of assets comprising the asset pool;

(6) Representation and warranties;

(7) Credit enhancements;

(8) Distribution of funds;

(9) Authorized investment of investible funds;

(10) Rights of the investor;

(11) Reports to investors; and

(12) Termination and final settlement.

The trust indenture shall include as annexes the servicing agreement between the trustee and the servicer and the underwriting agreement between the seller and the underwriter.

b. *Prospectus*. As a minimum requirement, it shall contain the following:

(1) Summary of the contents of the prospectus;

(2) Description of each class of certificates, including such matters as probable yields, payment dates and priority of payments;

(3) Description of the assets comprising the asset pool as well as the representations and warranties set forth by the originator and/or seller;

(4) Assumptions underlying the cash flow projections for each class of certificate;

(5) Description of any credit enhancement;

(6) Identity of the servicer; and

(7) Disclosure statements as required under Subsec. 4651Q.6.

c. *Specimen of application to purchase ABS*. It shall include the terms and conditions of the purchase and the disclosures required under Subsec. 4651Q.6.

d. *Specimen of certificate*. It shall indicate the features of the ABS and the disclosures required under Subsec. 4651Q.6.

§ 4651Q.5 ***(2008 - 4626Q.5) Minimum features of asset-backed securities.*** The ABS shall be pre-numbered and printed on security paper. The ABS shall be signed and authenticated by the trustee. They are transferable by endorsement of the certificate. The transfer shall be recorded in the books of the trustee, indicating the names of the parties to the transaction, the date of the transfer and the number of the certificate transferred.

The minimum denomination of any ABS shall be P10,000.

§ 4651Q.6 ***(2008 - 4626Q.6) Disclosures.*** The following disclosures must be provided in a conspicuous manner in any document inviting investment, application to purchase ABS and in the certificate itself:

a. The ABS do not represent deposit substitutes or liabilities of the originator, servicer or trustee and that they are not insured with PDIC;

b. The investor has investment risks;

c. The trustee does not guarantee the capital value of the ABS or the collectibility of the asset pool; and

d. The rights of an investor.

The investors shall be required to sign an acknowledgment indicating that they have read and understood the disclosures.

§ 4651Q.7 ***(2008 - 4626Q.7) Conveyance of assets***

a. The conveyance of the assets comprising the asset pool shall be done within the context of a true sale and, for this purpose, the seller may not retain in its books the ABS, except the residual certificate, if any.

b. The seller shall have no obligation to repurchase or substitute an asset or any part of the asset pool at any time, except in cases of a breach of representation or warranty, or under a revolving structure, to replace performing assets which have been paid out in part or in full.

c. The seller shall be under no obligation to provide additional assets to the SPT to maintain a coverage ratio of collateral to outstanding ABS. A breach of this requirement will be considered a credit enhancement and should be charged against capital. However, this will not apply to an asset pool conveyed under a revolving structure such as the securitization of credit card receivables.

d. Securitized assets shall be considered the subject of a true sale between the seller and the SPT. Sold assets shall be taken off the books of the seller and shall be transferred to the books of the SPT.

For accounting purposes, the transfer shall only be considered a true sale if the following three (3) conditions have been satisfied:

(1) the transferred assets have been isolated and put beyond the reach of the seller and its creditor;

(2) the SPT has the right to pledge or exchange its interest in the assets; and

(3) the seller does not effectively maintain control over the transferred assets by any concurrent agreement.

e. All expenses incidental to underwriting, conveyance of the asset pool including expenses for credit enhancement may be paid by the originator/seller:

Provided, That no further expenses shall be borne by the originator/seller after the asset pool has been conveyed to the SPT.

§ 4651Q.8 ***(2008 - 4626Q.8) Representations and warranties***

a. Standard representations and warranties refer to an existing state of facts that the originator, seller or servicer can either control or verify with reasonable due diligence at the time the assets are sold. Any breach of representation or warranty may give rise to legal recourse.

b. The representations or warranties shall be clear and explicit and, in particular, shall not relate to the future creditworthiness of the assets in the asset pool or the performance of the SPT or the securities issued.

c. Any agreement to pay damages as a result of breach of warranties and representations shall hold only where:

(1) there is a well-documented negotiation of the agreement in good faith;

(2) the burden of proof for a breach of representation or warranty rests with the other party;

(3) damages are limited to the loss incurred as a result of the breach; and

(4) there is a written notice of claim specifying the basis for the claim.

The BSP shall be notified of any instance where a QB or its subsidiaries/affiliates has agreed to pay damages arising out of any breach of representation or warranty.

§ 4651Q.9 ***(2008 - 4626Q.9) Third party review.*** A due diligence review by an independent entity mutually agreed upon by the seller and the issuer shall be done before the assets are sold.

§ 4651Q.10 ***(2008 - 4626Q.10) Originator and seller***

a. The seller may itself be the originator, and may likewise be designated as the servicer.

b. The seller or originator shall deliver to the trustee all original documents or instruments with respect to each asset sold.

§ 4651Q.11 ***(2008 - 4626Q.11) Trustee and issuer***

a. The trustee shall be the trust department of a bank licensed to do business in the Philippines.

b. The trustee shall have the right to manage or administer the asset pool. The trustee shall see to it that necessary measures are taken to protect the asset pool.

c. The trustee shall undertake a performance review of the asset pool at least quarterly and shall prepare a report to investors indicating, among others, collections, fees and other expenses as well as defaults, which report shall be made available to the investors at anytime after thirty (30) days from end of the reference quarter.

d. The trustee shall initiate all civil actions including foreclosure of mortgaged properties to effect collection of receivables in the asset pool. The servicer or any other party may be designated by the trustee to perform such function on a case-by-case basis.

e. The trustee may invest the investible funds only in obligations issued and/or fully guaranteed by the government of the Republic of the Philippines or by the BSP and such other high-grade readily marketable debt securities as the BSP may approve.

f. The trustee shall designate a replacement of the servicer if the latter fails to satisfactorily perform its duties and responsibilities according to the terms and conditions of the servicing agreement.

§ 4651Q.12 ***(2008 - 4626Q.12) Servicer***

a. The servicer shall perform its duties according to the terms and conditions of the servicing agreement and such other written instructions as the trustee may issue on a case-by-case basis. Collections made by the servicer shall be remitted promptly

to the trustee or as may be agreed upon by the parties in the servicing agreement, but in no case shall the remittance period be longer than one (1) month.

b. The servicer shall prepare periodic reports as may be required by the trustee.

c. The servicer shall report to the trustee within thirty (30) days any borrower which fails to pay its debt at maturity date or any adverse development that may affect the collectibility of any loan account or receivable comprising the asset pool.

d. The servicer shall have no authority to waive penalties and charges except with a written authority from the trustee.

§ 4651Q.13 ***(2008 - 4626Q.13) Underwriter***

a. A UB or IH shall have written policies and procedures on underwriting of ABS.

b. The underwriter shall perform its functions according to the terms and conditions of the underwriting agreement.

c. An underwriter may deal in ABS, except those administered by its trust department, the trust departments of its subsidiaries/affiliates, the trust department of its parent bank or the trust department of its parent bank's subsidiaries/affiliates.

d. A UB/IH may act as underwriter, on a firm basis, of ABS except those administered by its trust department, the trust departments of its subsidiaries/affiliates, the trust department of its parent bank or the trust department of its parent bank's subsidiaries/affiliates.

e. The underwriter may not extend credit for the purpose of purchasing the ABS which such UB/IH underwrites or that which is underwritten by its subsidiaries/affiliates, its parent bank or its parent bank's subsidiaries/affiliates.

§ 4651Q.14 ***(2008 - 4626Q.14) Guarantor***

a. Only an entity the regular business of which includes the issuance of guarantees or similar undertaking may act as guarantor.

b. The guarantor must have the financial capacity to perform its responsibilities in accordance with the terms and conditions of the guarantee agreement. It shall submit to the trustee at least once in every six (6) months such financial reports as the trustee may require.

c. The originator or seller may not issue a counter-guarantee in favor of the guarantor.

§ 4651Q.15 (*2008 - 4626Q.15*) *Credit enhancement.* Credit enhancement may be provided in any of the following manner:

a. Standby letter of credit issued by an UB/KB other than the originator's/seller's subsidiary/affiliate, parent bank or the parent bank's subsidiary/affiliate, and trustee or its subsidiary/affiliate.

b. Surety bond issued by any insurance company other than the originator's/seller's subsidiary or affiliate, the subsidiary or affiliate of the originator's seller's parent bank and the trustee or its subsidiary/affiliate.

c. Guarantee issued by any entity other than the originator/seller or its subsidiary/affiliate, its parent bank or the parent bank's subsidiary/affiliate, and trustee or its subsidiary/affiliate.

d. Overcollateralization provided by the originator/seller wherein the assets conveyed to the SPT exceed the amount of securities to be issued.

Losses arising from overcollateralization shall be recognized by the originator/seller upfront. Such losses shall be treated as capital charges.

e. Spread account wherein the income from the underlying pool of receivables is made available to cover any shortfall in the repayment of ABS. The spread account shall be handled by the trustee which shall account for it separately. If not needed, this "spread" generally reverts to the holder of the residual certificate.

f. Subordinated securities that are lower ranking, or junior to other obligations

and are paid after claims to holders of senior securities are satisfied.

g. Other credit enhancements as may be approved by the Monetary Board.

To be consistent with the concept of a true sale, subordinated securities shall be sold to third party investors other than the originator's/seller's parent company or its subsidiary/affiliate and the trustee or its subsidiary/affiliate or, if held by the seller, capital charges should be booked upfront. Otherwise, the subordinated securities shall be treated as deposit substitute subject to legal reserves.

§ 4651Q.16 (*2008 - 4626Q.16) Clean-up call.* A *clean-up call* may be exercised by the seller once the outstanding principal balance of the receivable component of the asset pool falls to ten percent (10%) or less of the original principal balance of the asset pool. Where the asset pool includes foreclosed and other assets, such assets shall be included in the clean-up call and the consideration thereof shall be at current market value. Such a *clean-up call* shall not be considered recourse or in violation of Subsec. 4651Q.7 on conveyance of assets.

§ 4651Q.17 *(2008 - 4626Q.17) Prohibited activities*

a. The seller may not, under any circumstance, designate its trust department, the trust department of its subsidiaries/affiliates, the trust department of its parent bank or the trust department of its parent bank's subsidiaries/affiliates as trustee.

b. Any director, officer or employee of the originator, seller or servicer may not serve as a member of the board of directors or trust committee of the trustee or vice versa for the duration of the securitization.

c. The trust indenture shall not contain any stipulation whereby the seller, its subsidiaries/affiliates, its parent bank or the parent bank's subsidiaries/affiliates shall commit to extend any credit facility to the issuer and/or trustee.

d. The ABS shall not be eligible as collateral for a loan extended by a QB which originated/sold the underlying assets of such ABS.

e. The trust department of a bank that has discretion in the management of any trust or investment management account may not purchase for said trust/investment management account ABS administered by the trust department of the same bank, the trust department of such trustee's subsidiaries/affiliates, the trust department of such trustee's parent bank and the trust department of the parent bank's subsidiaries/affiliates.

The trustee may not designate its subsidiary/affiliate, its parent or the parent's subsidiaries/affiliates as servicer or vice versa.

§ 4651Q.18 (*2008 - 4626Q.18*) *Amendment.* Any amendment to the trust indenture shall require the prior approval of the BSP.

§ 4651Q.19 (*2008 - 4626Q.19*) *Miscellaneous provision.* Without prior approval of the BSP, any entity supervised by the BSP authorized to engage in trust and fiduciary business may act as trustee or servicer in a securitization scheme originated by an entity not supervised by the BSP: *Provided,* That the assets which are the subject of such securitization are existing in the books of the entity prior to securitization: *Provided, further*, That such entity acting as trustee or servicer is not a subsidiary/affiliate of the originator/seller, its parent bank or the parent bank's subsidiaries/affiliates or vice versa: *Provided, finally*, That such entity acting as trustee may not designate its subsidiaries/affiliates, its parent or the parent's subsidiaries/affiliates as servicer or vice versa.

§ 4651Q.20 (*2008 - 4626Q.20*) *Report to Bangko Sentral.* The trustee shall submit a report of every securitization scheme in formats to be prescribed by the BSP. The report shall be submitted to the appropriate department of the SES, within fifteen (15) business days after the end of every reference quarter. Such report shall be considered a *Category A* report for purposes of implementing fines in the submission of required reports pursuant to existing regulations.

Secs. 4652Q - 4698Q (Reserved)

C. GENERAL PROVISION ON SANCTIONS

Sec. 4699Q General Provision on Sanctions Unless otherwise provided, any violation of the provisions of this Part shall be subject to Sections 36 and 37 of R.A. No. 7653.

The guidelines for the imposition of monetary penalty for violations/offenses with sanctions falling under Section 37 of R.A. No. 7653 on QBs, their directors and/or officers are shown in *Appendix Q-39*.

PART SEVEN

ELECTRONIC OPERATIONS AND OTHER SERVICES

Section 4701Q Electronic Services. The following are the guidelines concerning electronic activities.

(Circular No. 649 dated 09 March 2009)

§ 4701Q.1 *Application.* QBs wishing to provide and/or enhance existing electronic services shall submit to the BSP an application describing the services to be offered/enhanced and how it fits the QB's overall strategy. This shall be accompanied by a certification signed by its president or any officer of equivalent rank and function to the effect that the QB has complied with the following minimum pre-conditions:

a. An adequate risk management process is in place to assess, control, monitor and respond to potential risks arising from the proposed electronic services;

b. A manual on corporate security policy and procedures exists that shall address all security issues affecting its electronic services, particularly the following:

(1) Authentication – establishes the identity of both the sender and the receiver; uses trusted third parties that verify identities in cyberspace;

(2) Non-repudiation – ensures that transactions cannot be repudiated or presents undeniable proof of participation by both the sender and the receiver in a transaction;

(3) Authorization – establishes and enforces the access rights of entities (both persons and/or devices) to specified computing resources and application functions; also locks out unauthorized entities from physical and logical access to the secured systems;

(4) Integrity – assures that data have not been altered; and

(5) Confidentiality – assures that no one except the sender and the receiver of the data can actually understand the data.

c. The system had been tested prior to its implementation and that the test results are satisfactory. As a minimum standard, appropriate systems testing and user acceptance testing should have been conducted; and

d. A business continuity planning process and manuals have been adopted which should include a section on electronic services channels and systems.

(Circular No. 649 dated 09 March 2009)

§ 4701Q.2 *Pre-screening of applicants*

a. The BSP, thru the Technical Working Group on Electronic Banking, shall pre-screen the overall financial condition as well as the applicant-QB's compliance with BSP rules and regulations based on the latest available Bank Performance Rating equivalent for QBs and Report of Examination (ROE) including CAMELS Rating.

b. The Working Group shall ensure that the applicant QB's overall financial condition can adequately support its electronic services that it shall have complied with certain comprehensive prudential requirements such as, but not limited to, the following:

(1) Minimum capital requirement and net worth to risk assets ratio;

(2) Satisfactory solvency, liquidity and profitability positions;

(3) CAMELS composite rating of at least "3", (this rating, however can be flexible depending on other circumstances prevailing), and with at least a moderate risk

assessment system (RAS) based on the latest regular examination.

(4) There are no uncorrected major findings/exceptions noted in the latest BSP examination.

(Circular No. 649 dated 09 March 2009)

§ 4701Q.3 *Approval in principle*

a. Based on the recommendation of the Technical Working Group on Electronic Banking, the Deputy Governor, SES, shall approve in principle the application so that QBs may immediately launch and/or enhance their existing electronic services.

b. QBs shall be informed of the conditional approval of the DG, SES and they shall in turn notify the BSP on the actual date of its launching/enhancement.

(Circular No. 649 dated 09 March 2009)

§ 4701Q.4 *Documentary requirements*

a. Within thirty (30) calendar days from such launching/enhancement, QBs shall submit to the BSP thru the SDC for evaluation, the following documentary requirements:

(1) A discussion on the services to be offered/enhanced, the business objectives for such services and the corresponding procedures, both automated and manual, offered through the electronic services channels;

(2) A description or diagram of the configuration of the QB's electronic services system and its capabilities showing:

(i) how the electronic services system is linked to other host systems or the network infrastructure in the QB;

(ii) how transaction and data flow through the network;

(iii) what types of telecommunications channels and remote access capabilities (e.g., direct modem dial-in, internet access, or both) exist; and

(iv) what security controls/measures are installed;

(3) A list of software and hardware components indicating the purpose of the software and hardware in the electronic services infrastructure;

(4) A description of the security policies and procedures manual containing:

(i) description of the QB's security organization;

(ii) definition of responsibilities for designing, implementing, and monitoring information security measures; and

(iii) established procedures for evaluating policy compliance, enforcing disciplinary measures and reporting security violations;

(5) A brief description of the contingency and disaster recovery plans for electronic facilities and event scenario/ problem management plan/program to resolve or address problems, such as complaints errors and intrusions and the availability of back-up facilities;

(6) Copy of contract with the communications carrier, arrangements for any liability arising from breaches in the security of the system or from unauthorized/ fraudulent transactions;

(7) Copy of the maintenance agreements with the software/hardware provider/s; and

(8) Latest report on the periodic review of the system, if applicable.

b. If after the evaluation of the submitted documents, the Working Group has still some unresolved issues and gray areas, the QB may be required to make a presentation of its electronic transactions to BSP.

(Circular No. 649 dated 09 March 2009)

§ 4701Q.5 *Conditions for Monetary Board approval.* Upon completion of evaluation, the appropriate recommendation shall be made to the Monetary Board. The following shall be the standard conditions for approval:

a. Existence at all times of appropriate top-level risk management oversight;

b. Operation of electronic system outsourced to a third party service provider taking into consideration the existence of adequate security controls and the observance of confidentiality [as required in R.A. No. 1405 (Bank Secrecy Law)] of customer information;

c. Adoption of measures to properly educate customers on safeguarding of user ID, PIN and/or password, use of QB's products/services, actual fees/QB charges thereon and problem/error resolution procedures;

d. Clear communication with its customers in connection with the terms and condition which would highlight how any losses from security breaches, systems failure or human error will be settled between the QB and its customers;

e. Customer's acknowledgement in writing that they have understood the terms and conditions and the corresponding risks that entail in availing electronic service;

f. The QB's oversight process shall ensure that business expansion shall not put undue strains on its systems and risk management capability;

g. The establishment of procedures for the regular review of the QB's security arrangements to ensure that such arrangements remain appropriate having regard to the continuing developments in security technology;

h. Strict adherence to BSP regulations on fund transfers in cases where clients use the electronic services to transfer funds;

i. The electronic service shall not be used for money laundering or other illegal activities that will undermine the confidence of the public; and

j. The BSP shall be notified in writing thirty (30) days in advance of any enhancements that may be made to the online electronic service.

(Circular No. 649 dated 09 March 2009)

§ 4701Q.6 ***Requirements for quasi-banks with pending applications***. The same procedure and requirements stated in the foregoing shall apply to all QBs with pending applications with the BSP, except on the submission of the documents enumerated in Subsec. 4701Q.4. QBs which have already submitted all the required information/documents need not comply with this requirement.

(Circular No. 649 dated 09 March 2009)

§ 4701Q.7 ***Exemption.*** Electronic services that are purely informational in nature are exempted from these regulations: *Provided, however,* That should such services be upgraded to transactional service, then prior BSP approval shall be required.

(Circular No. 649 dated 09 March 2009)

§ 4701Q.8 ***Transitory provision.*** QBs with existing electronic services but do not qualify as a result of the pre-screening process mentioned in Subsec. 4701Q.2, shall be given three (3) months from 21 December 2000, within which to show proof of improved overall financial condition and/or substantial compliance with BSP's prudential requirements, otherwise, their electronic activities will be temporarily suspended until such time that the same have been complied with.

(Circular No. 649 dated 09 March 2009)

§§ 4701Q.9 - 4701Q.11 ***(Reserved)***

§ 4701Q.12 ***Sanctions.*** For failure to seek BSP approval before launching/ enhancing/implementing electronic services, and/or submit within the prescribed deadline the required information/documents, the following monetary penalties and/or suspension of electronic activities or both, shall be imposed on erring QBs and/or its officers:

	Monetary Penalties	Amount
a.	For responsible officer/s and/or director/s - for failure to seek prior BSP approval and/or for non-submission/delayed submission of required information/documents	P200,000 (one-time penalty)
b.	On the QB - for failure to seek prior BSP aproval and/or for non-submission/delayed submission of required information documents	P30,000 per day starting from the day the offense was committed up to the time the same was corrected

(Circular No. 649 dated 09 March 2009)

§ 4701Q.13 *Outsourcing of internet and mobile electronic services.* Outsourcing of internet and mobile electronic services shall be governed by Item *"c"* of *Appendix Q-37*.
(Circular No. 649 dated 09 March 2009)

Secs. 4702Q - 4779Q (Reserved)

Sec. 4780Q Issuance and Operations of Electronic Money. The following guidelines shall govern the issuance of electronic money (e-money) and the operations of electronic money issuers (EMIs).
(Circular No. 649 dated 09 March 2009)

§ 4780Q.1 *Declaration of policy.* It is the policy of the BSP to foster the development of efficient and convenient retail payment and fund transfer mechanism in the Philippines. The availability and acceptance of e-money as a retail payment medium will be promoted by providing the necessary safeguards and controls to mitigate the risks associated in an e-money business.
(Circular No. 649 dated 09 March 2009)

§ 4780Q.2 *Definitions*

E-money shall mean monetary value as represented by a claim on its issuer, that is -

a. electronically stored in an instrument or device;

b. issued against receipt of funds of an amount not lesser in value than the monetary value issued;

c. accepted as a means of payment by persons or entities other than the issuer;

d. withdrawable in cash or cash equivalent; and

e. issued in accordance with this Section.

Electronic money issuer (EMI) shall be classified as follows:

a. Banks (hereinafter called EMI-Bank);

b. NBFI supervised by the BSP (hereinafter called EMI-NBFI); and

c. Non-bank institutions registered with the BSP as a money transfer agent under Sec. 4511N of the MORNBFI (hereinafter called EMI-Others).

For purposes of this Section:

a. *Electronic instruments or devices* shall mean cash cards, e-wallets accessible via mobile phones or other access device, stored value cards, and other similar products.

b. E-money issued by QBs shall not be considered as deposits.
(Circular No. 649 dated 09 March 2009)

§ 4780Q.3 *Prior Bangko Sentral approval*. QBs planning to be an EMI-NBFI shall comply with the requirements of Sec. 4701Q and Sec. 4162Q, when applicable.
(Circular No. 649 dated 09 March 2009)

§ 4780Q.4 *Common provisions.* The following provisions are applicable to all EMIs:

a. E-money instrument issued shall be subject to aggregate monthly load limit of P100,000 unless a higher amount has been approved by BSP. In case an EMI issues several e-money instruments to a person (e-money holder), the total amount loaded in all the e-money instruments

shall be consolidated in determining compliance with the aggregate monthly load limit;

b. EMIs shall put in place a system to maintain accurate and complete record of e-money instruments issued, the identity of e-money holders, and the individual and consolidated balances thereof. The system must have the capability to monitor the movement of e-money transactions and link e-money instruments issued to common e-money holders. The susceptibility of a system to intentional or unintentional misreporting of transactions and balances shall be sufficient ground for imposition by the BSP of sanctions, as may be applicable.

c. E-money may only be redeemed at face value. It shall not earn interest nor rewards and other similar incentives convertible to cash, nor be purchased at a discount. E-money is not considered a deposit, hence, it is not insured with the PDIC.

d. EMIs shall ensure that e-money instruments clearly identify the issuer who is ultimately responsible to the e-money holders. This shall be communicated to the client who shall acknowledge the same in writing.

e. It is the responsibility of EMIs to ensure that their distributors/e-money agents comply with all applicable requirements of the Anti-Money Laundering laws, rules and regulations.

f. EMIs shall provide an acceptable redress mechanism to address the complaints of its customers.

g. EMIs shall disclose in writing and its customers shall signify agreement to the information embodied in Item "*c*" above upon their participation in the e-money system. In addition, it shall provide clear guidance in English and Filipino on consumers' right of redemption, including conditions and fees for redemption, if any. Information on available redress procedures for complaints together with the address and contact information of the issuer shall also be provided.

h. Prior to the issuance of e-money, EMIs should ensure that the following minimum systems and controls are in place:

(1) Sound and prudent management, administrative and accounting procedures and adequate internal control mechanisms;

(2) Properly-designed computer systems which are thoroughly tested prior to implementation;

(3) Appropriate security policies and measures intended to safeguard the integrity, authenticity and confidentiality of data and operating processes;

(4) Adequate business continuity and disaster recovery plan; and

(5) Effective audit function to provide periodic review of the security control environment and critical systems.

i. EMIs shall provide the SDC quarterly statements containing, among others, information on investments, volume of transactions, total outstanding e-money balances, and liquid assets in such forms as may be prescribed later on.

j. EMIs shall notify BSP in writing of any change or enhancement in the e-money facility thirty (30) days prior to implementation. If said change or enhancement requires prior BSP approval, the same shall be evaluated accordingly. Any change or enhancement that shall expand the scope or change the nature of the e-money instrument shall be subject to prior approval of the Deputy Governor, SES. These changes or enhancements may include the following:

(1) Additional capabilities of the e-money instrument/s, like access to new

channels (e.g. inclusion of internet channel in addition to merchant Point of Sale terminals);

(2) Change in technology service providers and other major partners in the e-money business (excluding partner merchants), if any; and

(3) Other changes or enhancements.

(Circular No. 649 dated 09 March 2009)

§ 4780Q.5 ***Quasi-bank license requirement.*** EMI-NBFIs and EMI-Others that engage in lending activities must secure a quasi-banking license from the BSP.

(Circular No. 649 dated 09 March 2009)

§ 4780Q.6 ***Sanctions.*** Monetary penalties and other sanctions for the following violations committed by EMI-NBFIs shall be imposed:

Nature of Violation/ Exception	Sanction/Penalties
1. Issuing e-money without prior BSP approval	Applicable penalties under Sections 36 & 37 of R.A. No. 7653; Watchlisting of owners/partners/ principal officers
2. Violation of any of the provisions of R.A. No. 9160 (Anti-Money Laundering Law of 2001 as amended by R.A.No. 9194) and its implementing rules and regulations	Applicable penalties prescribed under the Act
3. Violation/s of this Section	Penalties and sanctions under the abovementioned laws and other applicable laws rules and regulations

In addition, the susceptibility of a system to intentional or unintentional misreporting of transactions and balances shall be sufficient ground for appropriate BSP action or imposition of sanctions, whenever applicable.

(Circular No. 649 dated 09 March 2009)

§ 4780Q.7 ***Transitory provisions*** EMI-NBFIs granted an authority to issue e-money prior to 26 March 2009 may continue to exercise such authority: *Provided,* That it shall submit to the BSP, within one (1) month from 26 March 2009 a certification signed by the President or Officer with equivalent rank and function that it is in compliance with all the applicable requirements of this Section. Otherwise, they are required to submit within the same period the measures they will undertake, with the corresponding timelines, to conform to the provisions that they have not complied with, subject to BSP approval.

(Circular No. 649 dated 09 March 2009)

§§ 4780Q.8 - 4780Q.10 ***(Reserved)***

§ 4780Q.11 ***Outsourcing of services by Electronic Money Issuers (EMIs) to Electronic Money Network Service Providers (EMNSP).*** The guidelines on outsourcing of services by Electronic Money Issuers (EMIs) to Electronic Money Network Service Providers (EMNSP) are shown in *Appendix Q-54*.

Sanctions. Violations committed by EMIs pertaining to outsourcing activities to EMNSP shall be subject to monetary penalties as graduated under *Appendix Q-39* and/or other non-monetary sanctions under Section 37 of RA No. 7653.

Transitory provisions. EMIs that were granted an authority to outsource their E-money activities to an EMNSP may continue to exercise such authority provided that they have to conform to the provisions of *Appendix Q-54* within a six-month period from 20 January 2011.

(Circular 704 dated 22 December 2010)

Secs. 4781Q - 4798Q (Reserved)

Sec. 4799Q General Provision on Sanctions. Any violation of the provisions of this Part shall be subject to Sections 36 and 37 of R.A. No. 7653.

The guidelines for the imposition of monetary penalty for violations/offenses with sanctions falling under Section 37 of R.A. No. 7653 on QBs, their directors and/or officers are shown in *Appendix Q-39*.

PART EIGHT

ANTI - MONEY LAUNDERING REGULATIONS

Section 4801Q *(2008 - 4691Q & App. Q-23)* Prevention of Money Laundering, Customer Identification Requirements and Record Keeping. Banks, OBUs, QBs, trust entities, NSSLAs, pawnshops, and all other institutions, including their subsidiaries and affiliates supervised and/or regulated by the BSP, otherwise known as "covered institutions (CIs)" shall comply with the provisions of R.A. No. 9160, as amended, otherwise known as the "Anti-Money Laundering Act of 2001" and its Revised Implementing Rules and Regulations (IRRs) in *Appendix Q-25*.

CIs shall strictly comply with the following rules and regulations on anti-money laundering.

(As amended by Circular Nos. 612 dated 13 June 2008 and 564 dated 03 April 2007)

§ 4801Q.1 *(2008 - App. Q-23) Customer identification.* CIs shall establish and record the true identity of its clients based on official documents. They shall maintain a system of verifying the true identity of their clients and, in case of corporate clients, require a system of verifying their legal existence and organizational structure, as well as the authority and identification of all persons purporting to act on their behalf.

The guidelines on Customer Due Diligence for QBs issued by the BASEL Committee on Banking Supervision which highlights the Know-Your-Customer (KYC) standards to be observed in the design of KYC programs are shown in *Annex Q-23c*.

The guidelines on the Account Opening and Customer Identification issued by the BASEL Committee on Banking Supervision represent the starting point, which can be used by banks in the area of customer identification are shown in *Annex Q-23d*.

When establishing business relations or conducting transactions (particularly opening of deposit accounts, accepting deposit substitutes, entering into trust and other fiduciary transactions, renting of safety deposit boxes, performing remittances and other large cash transactions) CIs should take reasonable measures to establish and record the true identity of their clients. Said client identification may be based on official or other reliable documents and records.

a. In cases of corporate and other legal entities, the following measures should be taken, when necessary:

(1) Verification of the legal existence and structure of the client from the appropriate agency or from the client itself or both, proof of incorporation, including information concerning the customer's name, legal form, address, directors, principal officers and provisions regulating the power behind the entity.

(2) Verification of the authority and identification of the person purporting to act on behalf of the client.

b. In case of doubt as to whether their purported clients or customers are acting for themselves or for another, reasonable measures should be taken to obtain the true identity of the persons on whose behalf an account is opened or a transaction conducted.

c. The provisions of existing laws to the contrary notwithstanding, anonymous accounts, accounts under fictitious names, and all other similar accounts shall be absolutely prohibited. In case where numbered accounts is allowed (i.e., peso and foreign currency non-checking numbered accounts), CIs should ensure

that the client is identified in an official or other identifying documents.

The BSP may conduct annual testing solely limited to the determination of the existence and the identity of the owners of such accounts.

CIs shall phase out within a period of one (1) year from 02 April 2001 or upon their maturity, whichever is earlier, anonymous accounts or accounts under fictitious names as well as numbered accounts being kept or managed by them, which are not expressly allowed under existing law.

d. The identity of existing clients or beneficial owners of deposits and other funds held or being managed by CIs should be renewed/updated at least every other year.

e. All records of all transactions of CIs shall be maintained and safely stored for five (5) years from the dates of transactions. With respect to closed accounts, the records on customer identification, account files and business correspondence, shall be preserved and safely stored for at least five (5) years from the dates when they were closed.

Such records must be sufficient to permit reconstruction of individual transactions so as to provide, if necessary, evidence for prosecution of criminal behaviour.

f. Special attention should be given to all complex, unusual large transactions, and all unusual patterns of transactions, which have no apparent or visible lawful purpose.The background and purpose of such transactions should, as far as possible, be examined, the findings established in writing, and be available to help supervisors, auditors and law enforcement agencies.

g. CIs should not, or should at least avoid, transacting business with criminals. Reasonable measures should be adopted to prevent the use of their facilities for laundering of proceeds of crimes and other illegal activities.

§ 4801Q.2 ***(Reserved)***

§ 4801Q.3 ***(2008 - App. Q - 23) Programs against money laundering.*** Programs against money laundering should be developed. These programs, should include, as a minimum:

a. The development of internal policies, procedures and controls, including the designation of compliance officers at management level, and adequate screening procedures to ensure high standards when hiring employees;

b. An ongoing employee training program; and

c. An audit function to test the system.

§ 4801Q.4 ***(2008 - App. Q - 23) Submission of plans of action.*** CIs shall submit a plan of action on how to comply with the requirements of Subsecs. 4801Q.1, 4801Q.3 and 4801Q.5 within thirty (30) business days from 31 July 2000 or from opening of the institution.

(As amended by Circular No. 661 dated 01 September 2009)

§ 4801Q.5 ***(2008 - App. Q-23) Required reporting of certain transactions.***[1] If there is reasonable ground to believe that the funds are proceeds of an unlawful activity as defined under R.A. No. 9160 and/or its IRRs, the transactions involving such funds or attempts to transact the same, should be reported to the Anti-Money Laundering Council (AMLC) in accordance with Rules 5.2 and 5.3 of the AMLA IRRs.

a. *Report on suspicious transactions*.[2] Banks shall report covered transactions and suspicious transactions, as defined in Rules 5.2 and 5.3 of the AMLA IRRs, to the AMLC using the forms prescribed by the AMLC. Reportable transactions shall include the following:

[1] See amendments in *Appendix Q-23b*.
[2] Amended by AMLC Resolution No. 292 dated 30 November 2003 *(Annex Q-23b)*.

(1) Outward remittances without visible lawful purpose;

(2) Inward remittances without visible lawful purpose or without underlying trade transactions;

(3) Unusual purchases of foreign exchange without visible lawful purpose;

(4) Unusual sales of foreign exchange whose sources are not satisfactorily established;

(5) Complex, unusual large transactions, and all unusual patterns of transactions, which have no apparent or visible lawful purpose;

(6) Funds being managed or held as deposit substitutes if there is reasonable ground to believe that the same are proceeds of criminal and other illegal activities; and

(7) Suspicious Transaction Indicators or "Red Flags" as a Guide in the Submission to the AMLC of Reports of Suspicious Transactions Relating To Potential or Actual Financing of Terrorism.

(a) Wire transfers between accounts, without visible economic or business purpose, especially if the wire transfers are effected through countries which are identified or connected with terrorist activities.

(b) Sources and/or beneficiaries of wire transfers are citizens of countries which are identified or connected with terrorist activities.

(c) Repetitive deposits or withdrawals that cannot be explained or do not make sense.

(d) Value of the transaction is over and above what the client is capable of earning.

(e) Client is conducting a transaction that is out of the ordinary for his known business interest.

(f) Deposits being made by individuals who have no known connection or relation with the account holder.

(g) An individual receiving remittances, but has no family members working in the country from which the remittance is made.

(h) Client was reported and/or mentioned in the news to be involved in terrorist activities.

(i) Client is under investigation by law enforcement agencies for possible involvement in terrorist activities.

(j) Transactions of individuals, companies or NGOs that are affiliated or related to people suspected of being connected to a terrorist group or a group that advocates violent overthrow of a government.

(k) Transactions of individuals, companies or NGOs that are suspected as being used to pay or receive funds from revolutionary taxes.

(l) The NGO does not appear to have expenses normally related to relief or humanitarian effort.

(m) The absence of contributions from donors located within the country of origin of the NGO.

(n) A mismatch between the pattern and size of financial transactions on the one hand and the stated purpose and activity of the NGO on the other.

(o) Incongruities between apparent sources and amount of funds raised or moved by the NGO.

(p) Any other transaction that is similar, identical or analogous to any of the foregoing.

(8) All other suspicious transactions/ activities which can be reported without violating any law.

The report on suspicious transactions shall provide the following minimum information:

(a) Name or names of the parties involved.

(b) A brief description of the transaction or transactions.

(c) Date or date the transaction(s) occurred.

(d) Amount(s) involved in every transaction.

(e) Such other relevant information which can be of help to the authorities should there be an investigation.

b. *Exemption from Bank Secrecy Law* When reporting covered transactions to the AMLC, CIs and their officers, employees, representatives, agents, advisors, consultants or associates shall not be deemed to have violated R.A. No. 1405, as amended; R.A. No. 6426, as amended; R.A. No. 8791 and other similar laws, but are prohibited from communicating, directly or indirectly, in any manner or by any means, to any person the fact that a covered transaction report was made, the contents thereof, or any other information in relation thereto. In case of violation thereof, the concerned officer, employee, representative, agent, advisor, consultant or associate of the CI, shall be criminally liable. However, no administrative, criminal or civil proceedings, shall lie against any person for having made a covered transaction report in the regular performance of his duties and in good faith, whether or not such reporting results in any criminal prosecution under R.A. No. 9160 or any other Philippine law.

c. *Prohibition from disclosure of the covered transaction report*. When reporting covered transactions to the AMLC, CIs and their officers, employees, representatives, agents, advisors, consultants or associates are prohibited from communicating, directly or indirectly, in any manner or by any means, to any person, entity, the media, the fact that a covered transaction report was made, the contents thereof, or any other information in relation thereto. Neither may such reporting be published or aired in any manner or form by the mass media, electronic mail, or other similar devices. In case of violation thereof, the concerned officer, employee, representative, agent, advisor, consultant or associate of the CI, or media shall be held criminally liable.

(As amended by CL-2009-037 dated 04 May 2009)

§ 4801Q.6 ***(2008 - App. Q-23a) Certification of compliance with anti-money laundering regulations.*** CI shall submit annually to the BSP thru the appropriate department of the SES a certification (*Annex Q-23a)* signed by the president or officer of equivalent rank and by their compliance officer to the effect that they have monitored compliance with existing anti-money laundering regulations.

The certification shall be submitted in accordance with *Appendix Q-3* and shall be considered a *Category A-2* report.

(As amended by Circular No. 661 dated 01 September 2009

§ 4801Q.7 ***(Reserved)***

Secs. 4802Q - 4881Q (Reserved)

Sec. 4882Q ***(2008 - 4691Q.9)*** **Sanctions and Penalties**

a. Whenever a CI violates the provisions of Section 9 of R.A. No. 9160, as amended, or of the preceding Sections, the officer(s) or other persons responsible for such violation shall be punished by a fine of not less than P50,000 nor more than P200,000 or by imprisonment of not less than two (2) years nor more than ten (10) years, or both, at the discretion of the court pursuant to Section 36 of R.A. No. 7653.

b. Without prejudice to the criminal sanctions prescribed above against the culpable persons, the Monetary Board may, at its discretion, impose upon any CI, its directors and/or officers for any violation of Section 9 of R.A. No. 9160, as amended, the administrative sanctions provided under Section 37 of R.A. No. 7653.

Secs. 4883Q - 4894Q (Reserved)

Sec. 4895Q ***(2008 - 4695Q)*** **Valid Identification Cards for Financial Transactions.** The following guidelines govern the acceptance of valid ID cards for all types of financial transactions by

QBs, including financial transactions involving overseas Filipino workers (OFWs), in order to promote access of Filipinos to services offered by formal FIs, particularly those residing in the remote areas, as well as to encourage and facilitate remittances of OFWs through the banking system:

a. Clients who engage in a financial transaction with CIs for the first time shall be required to present the original and submit a clear copy of at least one (1) valid photo-bearing ID document issued by an official authority.

For this purpose, the term *official authority* shall refer to any of the following:

(1) Government of the Republic of the Philippines;

(2) Its political subdivisions and instrumentalities;

(3) GOCCs; and

(4) Private entities or institutions registered with or supervised or regulated either by the BSP or SEC or IC.

Valid IDs include the following:

(a) Passport;
(b) Driver's license;
(c) PRC ID;
(d) NBI clearance;
(e) Police clearance;
(f) Postal ID;
(g) Voter's ID;
(h) Barangay certification;
(i) GSIS e-Card;
(j) SSS card;
(k) Senior Citizen card;
(l) OWWA ID;
(m) OFW ID;
(n) Seaman's Book;
(o) Alien Certification of Registration/ Immigrant Certificate of Registration;
(p) Government office and GOCC ID, (e.g., AFP, HDMF IDs);
(q) Certification from the NCWDP;
(r) DSWD certification;
(s) IBP ID;
(t) Company IDs issued by private entities or institutions registered with or supervised or regulated either by the BSP, SEC or IC; and
(u) Passports issued by foreign governments.

b. Students who are beneficiaries of remittances/fund transfers and who are not yet of voting age, may be allowed to present the original and submit a clear copy of one (1) valid photo-bearing school ID duly signed by the principal or head of the school.

c. QBs shall require their clients to submit a clear copy of the one (1) valid ID on a one-time basis only, or at the commencement of a business relationship. They shall require their clients to submit an updated photo and other relevant information whenever the need for it arises.

The foregoing shall be in addition to the customer identification requirements under Rule 9.1.c of the Revised IRRs of R.A. No. 9160, as amended *(Appendix Q-25)*.

For purposes of this Section, financial transactions may include remittances, among others, as falling under the definition of transaction. Under the Anti-Money Laundering Act of 2001, as amended, a *financial transaction* is any act establishing any right or obligation or giving rise to any contractual or legal relationship between the parties thereto. It also includes any movement of funds by any means with a CI.

(Circular No. 564 dated 03 April 2007 as amended by Circular Nos. 657 dated 16 June 2009 and 608 dated 20 May 2008)

Secs. 4896Q - 4898Q (Reserved)

Sec. 4899Q *(2008 - 4699Q)* General Provision on Sanctions. Unless otherwise provided, any violation of the provisions of this Part shall be subject to Sections 36 and 37 of R.A. No. 7653.

The guidelines for the imposition of monetary penalty for violations/offenses with sanctions falling under Section 37 of R.A. No. 7653 on QBs, their directors and/or officers are shown in *Appendix Q-39*.

PART NINE

OTHER NON-BANK OPERATIONS

A. BANKING FEES/CHARGES

Sec. 4901Q (Reserved)

§ 4901Q.1 ***(2008 - 4652Q) Annual Fees on quasi-banks.*** QBs shall contribute to the BSP an annual fee to help defray the cost of maintaining the appropriate department of the SES.

For purposes of computing the annual fees chargeable against QBs, the term *Total Assessable Assets* shall be the amount referred to as the total assets under Section 28 of R.A. No. 7653 (end-of-quarter total assets per balance sheet, after deducting cash on hand and amounts due from banks, including the BSP and banks abroad) plus Trust Department accounts.

Average Assessable Assets (AAAs) shall be the summation of end-of-quarter total assessable assets divided by the number of quarters in operation during the particular assessment period.

The annual fees for QBs beginning assessable year 2010 shall be one thirty-second (1/32) of one percent (1%) multiplied by their AAAs.

Annual fees to be collected from QBs shall be debited from their respective deposits with the BSP by the BSP Comptrollership Department upon receipt of the notice of the assessment from the appropriate department of the SES.

Where the deposit account is insufficient to cover the assessment fee, the BSP shall bill the QB for the full amount of the annual fee or for the balance thereof not covered by its deposit account, as the case may be.

Within thirty (30) calendar days from receipt of the bill, the QB shall make the corresponding remittance to the BSP. Failure to pay the bill within the prescribed period shall subject the QB to administrative sanctions.

The guidelines in the collection of the annual supervisory fees for the years 2010 are provided in *Appendix Q-51*.

(As amended by M-2010-013 dated 31 May 2010, Circular No. 687 dated 21 May 2010, M-2009-046 dated 17 November 2009, M-2009-004 dated 12 February 2009 and Circular No. 643 dated 10 February 2009)

Sec. 4902Q ***(2008 - 4653Q)*** **Payment of Fines and Other Charges.** The following regulations shall govern the payment of fines and other charges by QBs.

§ 4902Q.1 ***(2008 - 4653Q.1) Guidelines on the imposition of monetary penalties*** The following are the guidelines on the imposition of monetary penalties on QBs, their directors and/or officers:

a. *Definition of terms*. For purposes of the imposition of monetary penalties, the following definitions are adopted:

(1) *Continuing offenses/violations* are acts, omissions or transactions entered into, in violation of laws, BSP rules and regulations, Monetary Board directives, and orders of the Governor which persist from the time the particular acts were committed or omitted or the transactions were entered into until the same were corrected/rectified by subsequent acts or transactions. They shall be penalized on a per calendar day basis from the time the acts were committed/omitted or the transactions were effected up to the time they were corrected/rectified.

(2) *Transactional offenses/violations* are

acts, omissions or transactions entered into in violation of laws, BSP rules and regulations, Monetary Board directives, and orders of the Governor which cannot be corrected/rectified by subsequent acts or transactions. They shall be meted with one-time monetary penalty on a per transaction basis.

(3) *Continuing penalty* refers to the monetary penalty imposed on continuing offenses/violations on a per calendar day basis reckoned from the time the offense/violation occurred or was committed until the same was corrected/rectified.

(4) *Transactional penalty* refers to a one (1)-time penalty imposed on a transactional offense/violation.

b. *Basis for the computation of the period or duration of penalty*. The computation of the period or duration of all penalties shall be based on calendar days. For this purpose the terms "*per banking day*", "*per business day*", "*per day*" and/or "*a day*" as used in the Manual, and other BSP rules and regulations shall mean "*per calendar day*" and/or "*calendar day*" as the case may be.

c. *Additional charge for late payment of monetary penalty*. Late payment of monetary penalty shall be subject to an additional charge of six percent (6%) per annum to be reckoned from the business day immediately following the day said penalty becomes due and payable up to the day of actual payment. The penalty shall become due and payable fifteen (15) calendar days from receipt of the Statement of Account from the BSP. For QBs which maintain DDA with the BSP, penalties which remain unpaid after the lapse of the fifteen (15)-day period shall be automatically debited against their corresponding DDA on the following business day without additional charge. If the balance of the concerned QB's DDA is insufficient to cover the amount of the penalty, said penalty shall already be subject to an additional charge of six percent (6%) per annum to be reckoned from the business day immediately following the end of said fifteen (15)-day period up to the day of actual payment.

d. *Appeal or request for reconsideration*. A one (1)-time appeal or request for reconsideration on the monetary penalty approved by the Governor/Monetary Board to be imposed on the QB, its directors and/or officers shall be allowed: *Provided*, That the same is filed with the appropriate department of the SES within fifteen (15) calendar days from receipt of the Statement of Account/billing letter. The appropriate department of the SES shall evaluate the appeal or request for reconsideration of the QB/individual and make recommendations thereon within thirty (30) calendar days from receipt thereof. The appeal or request for reconsideration on the monetary penalty approved by the Governor/Monetary Board shall be elevated to the Monetary Board for resolution/decision. The running of the penalty period in case of continuing penalty and/or the period for computing additional charge shall be interrupted from the time the appeal or request for reconsideration was received by the appropriate department of the SES up to the time that the notice of the Monetary Board decision was received by the QB/individual concerned.

(As amended by Circular Nos.662 dated 09 September 2009 and 585 dated 15 October 2007)

§ 4902Q.2 ***(2008 - 4653Q.2) Payment of fines.*** QBs shall, within fifteen (15) calendar days from receipt of the statement of account from the BSP, pay the fines for reserve deficiency, reportorial delay/deficiency, refusal to permit examination, or failure to comply with, or violation of, any law or any order, instruction or regulation issued by the Monetary Board, or any order, instruction or ruling by the Governor.

For QBs which maintain DDAs with the BSP, fines which are unpaid after the

lapse of the fifteen (15)-day period shall be automatically debited against the corresponding DDA of the QB concerned: *Provided,* That if the balance of the entity's account is insufficient to cover the fines due, such fines shall be paid not later than the following business day. For the purpose of this Section, *business day* means a day on which the BSP head office and the head office of the QB are open for business. For uniform implementation of the above regulations, the procedural guidelines embodied in *Appendix Q-22* shall be observed.

(As amended by Circular Nos. 662 dated 09 September 2009 and 585 dated 15 October 2007)

§ 4902Q.3 *(Reserved)*

§ 4902Q.4 *(2008 - 4653Q.3) Check/ demand draft payments to the Bangko Sentral.* QBs shall make all check and demand draft payments for transactions other than those required to be paid through the QBs' DDA either to the BSP Cash Department or to the BSP Regional Offices and Branches. Such payments shall be accompanied by the appropriate form as shown in *Appendix Q-22a*. Payments not accompanied by the required payment forms shall be presumed to be additions to reserves and shall be credited to the DDA of the paying QB.

Check payments shall be value-dated when the check is cleared.

(As amended by Circular Nos. 662 dated 09 September 2009 and 585 dated 15 October 2007)

Sec. 4903Q (2008 - 4604Q) Underwriting by Investment Houses. Underwriting commitments and fees of IHs shall be subject to the rules issued by the SEC to implement the provisions of P.D. No. 129, as amended *(Appendix Q-18)*.

Secs. 4904Q - 4920Q (Reserved)

B. BANK AS COLLECTION/ REMITTANCE AGENTS

Sec. 4921Q *(2008 - 4660Q)* Disclosure of Remittance Charges and Other Relevant Information. It is the policy of the BSP to promote the efficient delivery of competitively-priced remittance services by banks and other remittance service providers by promoting competition and the use of innovative payment systems, strengthening the financial infrastructure, enhancing access to formal remittance channels in the source and destination countries, deepening the financial literacy of consumers, and improving transparency in remittance transactions, consistent with sound practices.

Towards this end, NBFIs under BSP supervision, including FXDs/MCs and RAs, providing overseas remittance services shall disclose to the remittance sender and to the recipient/beneficiary, the following minimum items of information regarding remittance transactions, as defined herein:

a. *Transfer/remittance fee* - charge for processing/sending the remittance from the country of origin to the country of destination and/or charge for receiving the remittance at the country of destination;

b. *Exchange rate* - rate of conversion from foreign currency to local currency, e.g., peso-dollar rate;

c. Exchange rate differential/spread - foreign exchange mark-up or the difference between the prevailing BSP reference/ guiding rate and the exchange/conversion rate;

d. *Other currency conversion charges* commissions or service fees, if any;

e. *Other related charges* - e.g., surcharges, postage, text message or telegram;

f. Amount/currency paid out in the *recipient country* - exact amount of money the recipient should receive in local currency or foreign currency; and

g. Delivery time to recipients/ *beneficiaries* - delivery period of remittance to beneficiary stated in number of days, hours or minutes.

Non-bank remittance service providers shall likewise post said information in their respective websites and display them prominently in conspicuous places within their premises and/or remittance/service centers.
(Circular No. 534 dated 26 June 2006)

Secs. 4922Q - 4930Q (Reserved)

C. CREDIT RATING AGENCIES

Sec. 4931Q *(2008 - 4657Q)* Recognition and Derecognition of Domestic Credit Rating Agencies for Quasi-Bank Supervisory Purposes. The following regulations shall govern the recognition and derecognition of domestic credit rating agencies (CRAs) for QB supervisory purposes.

§ 4931Q.1 *(2008 - 4657Q.1) Statement of policy.* The introduction in the financial market of new and innovative products create increasing demand for and reliance on CRAs by the industry players and regulators as well. As a matter of policy, the BSP wants to ensure that the reliance on credit ratings is not misplaced. The following rules and regulations that shall govern the recognition/derecognition of domestic CRAs for QB supervisory purposes.

§ 4931Q.2 *(2008 - 4657Q.2) Minimum eligibility criteria.* Only ratings issued by CRAs recognized by the BSP shall be considered for BSP QB supervisory purposes. The BSP, through the Monetary Board, may officially recognize a credit rating agency upon satisfaction of the following requirements:

a. *Organizational structure*

(1) A domestic CRA must be a duly registered company under the SEC; and

(2) A domestic CRA must have at least five (5) years track record in the issuance of reliable and credible ratings. In the case of new entrants, a probationary status may be granted: *Provided,* That the CRA employs professional analytical staff with experience in the credit rating business.

b. *Resources*

(1) Human Resources

(a) The size and quality of the CRA's professional analytical staff must have the capability to thoroughly and competently evaluate the assessed/rated entity's creditworthiness;

(b) The size of the CRA's professional analytical staff must be sufficient to allow substantial on-going contact with senior management and operational levels of assessed/rated entities as a routine component of the surveillance process;

(c) The CRA shall establish a Rating Committee composed of adequately qualified and knowledgeable individuals in the rating business, majority of whom must have at least five (5) years experience in credit rating business;

(d) The directors of the CRA must possess a high degree of competency equipped with the appropriate education and relevant experience in the rating business;

(e) The directors, officers, members of the rating committee and professional analytical staff of the CRA have not at any time been convicted of any offense involving moral turpitude or violation of the SRC; and

(f) The directors, officers, members of the rating committee and professional analytical staff of the CRA are not currently involved as a defendant in any litigation connected with violations of the SRC nor included in the BSP watchlist.

(2) Financial resources

(a) The CRA must have the financial capability to invest in the necessary technological infrastructure to ensure

speedy acquisition and processing of data/information and timely release of reliable and credible ratings; and

(b) The CRA must have financial independence that will allow it to operate free from economic and political pressures.

c. *Objectivity*

(1) The CRA must use a rigorous and systematic assessment methodology that has been established for at least one (1) year; however, a three (3)-year period is preferable;

(Next page is Part IX - Page 5)

(2) The assessment methodology of the CRA must be based both on qualitative and quantitative approaches; and

(3) The CRA must use an assessment methodology that is subject to on-going review and is responsive to changes in the operations of assessed/rated entities.

d. *Independence*

(1) The CRA must be free from control of and undue influence by the entities it assesses/rates;

(2) The assessment process must be free from ownership pressures to allow management to exercise independent professional judgement;

(3) Persons directly involved in the assessment process of the CRA are free from conflicts of interest with assessed/ rated entities, and

(4) The CRA does not assess/rate an associate entity.

e. *Transparency*

(1) A general statement of the assessment methodology used by the CRA should be publicly available;

(2) The CRA shall disseminate to the public thru a well-circularized publication, all assigned ratings disclosing whether the rating issued is solicited or unsolicited;

(3) The rationale of ratings issued and risk factors considered in the assessment should be made available to the public;

(4) The ratings issued by the CRA should be available both to domestic and foreign institutions with legitimate interest; and

(5) Publication of changes in ratings together with the basis for the change should be done on a timely basis.

f. *Disclosure requirements*

(1) Qualitative disclosures

(a) Definition of ratings along with corresponding symbols;

(b) Definition of what constitutes a default, time horizon within which a default is considered and measure of loss given a default;

(c) Material changes within the CRA (i.e., changes in management or organizational structure, rating personnel, modifications of rating practices, financial deterioration) that may affect its ability to provide reliable and credible ratings.

(2) Quantitative disclosures

(a) Actual default rates experienced in each rating category; and

(b) Rating transitions of assessed/rated entities over time (i.e., likelihood of an AAA credit rating transiting to AA etc. over time).

g. *Credibility*

(1) The CRA must have a general reputation of high standards of integrity and fairness in dealing with its clients and conducts its business in an ethical manner;

(2) The CRA is generally accepted by predominant users in the market (i.e., issuers, investors, bankers, FIs, securities traders); and

(3) The CRA must carry out its rating activities with due diligence to ensure ratings are fair and appropriate.

For purposes of this Section, a subsidiary refers to a corporation, more than fifty percent (50%) of the voting stock of which is owned or controlled directly or indirectly by the CRA while an affiliate refers to a corporation, not more than fifty percent (50%) but not less than ten percent (10%) of the voting stock of which is owned or controlled directly or indirectly by the CRA.

Control exists when the parent owns directly or indirectly through subsidiaries more than one-half (½) of the voting power of an enterprise unless, in exceptional circumstance, it can be clearly demonstrated that such ownership does not constitute control. Control may also exist even when ownership is one-half (½) or less of the voting power of an enterprise when there is:

(a) power over more than one-half (½) of the voting rights by virtue of an agreement with other stockholders;

(b) power to govern the financial and operating policies of the enterprise under a statute or an agreement;

(c) power to appoint or remove the majority of the members of the board of directors or equivalent governing body;

(d) power to cast the majority votes at meetings of the board of directors or equivalent governing body; or

(e) any other arrangement similar to any of the above.

h. *Internal compliance procedures*

(1) The CRA must have the necessary internal procedures to prevent misuse or unauthorized disclosure of confidential/ non-public information; and

(2) The CRA must have rules and regulations that prevent insider trading and other conflict of interest situations.

§ 4931Q.3 ***(2008 - 4657Q.3) Pre-qualification requirements.*** The application of a domestic CRA for BSP recognition shall be submitted to the appropriate department of the SES together with the following information/documents:

a. *An undertaking*

(1) That the CRA shall comply with regulations, directives and instructions which the BSP or other regulatory agency/ body may issue from time to time; and

(2) That the CRA shall notify the BSP in writing of any material changes within the organization (i.e., changes in management or organizational structure, rating personnel, modifications of its rating practices, financial deterioration) that may affect its ability to provide reliable and credible ratings.

b. *Other documents/information:*

(1) Brief history of the CRA, major rating activities handled including information on the name of the client, type of instruments rated, size and year of issue;

(2) Audited financial statements for the past three (3) years and such other information as the Monetary Board may consider necessary for selection purposes;

(3) For new entrants, employment of professional analytical staff with experience in the credit rating business;

(4) List of major stockholders/partners [owning at least ten percent (10%) of the voting stocks of the CRA directly or along with relatives within the 1st degree of consanguinity or affinity];

(5) List of directors, officers, members of the rating committee and professional analytical staff of the CRA; including their qualifications, experience related to rating activities, directorship and shareholdings in the CRA and in other companies, if any;

(6) List of subsidiaries and affiliates including their line of business and the nature of interest of the CRA in these companies;

(7) Details of the denial of a previous request for recognition, if any (i.e., application date, date of denial, reason for denial, etc.); and

(8) Details of all settled and pending litigations connected with the securities market against the CRA, its directors, officers, stockholders, members of the rating committee and professional analytical staff, if any.

§ 4931Q.4 ***(2008 - 4657Q.4) Inclusion in BSP list.*** The BSP will regularly circularize to all banks and NBFIs an updated list of recognized CRAs. The BSP, however, shall not be liable for any damage or loss that may arise from its recognition of CRAs to be engaged by users.

§ 4931Q.5 ***(2008 - 4657Q.5) Derecognition of credit rating agencies***

a. *Grounds for derecognition*. CRAs may be derecognized from the list of BSP recognized CRAs under the following circumstances:

(1) Failure to maintain compliance with the requirements under Subsec. 4657Q.2 or any willful misrepresentation in the information/documents required under Subsec. 4657Q.3;

(2) Involvement in illegal activities such as ratings blackmail; creation of a false market or insider trading; divulging any confidential information about a client without prior consent to a third party without legitimate interest; indulging in unfair competition (i.e., luring clients of another rating agency by assuring higher ratings, etc.); and

(3) Any violation of applicable laws, rules and regulations.

b. *Procedure for derecognition*. A CRA shall only be derecognized upon prior notice and after being given the opportunity to defend itself.

§ 4931Q.6 ***(2008 - 4657Q.6) Recognition of PhilRatings as domestic credit rating agency for bank supervisory purposes*** Credit ratings assigned by Philippine Rating Services Corporation (PhilRatings) may be used, among others, for determining appropriate risk weights in ascertaining compliance with existing rules and regulations on risk-based capital requirements.

Sec. 4932Q ***(2008 - 4659Q)*** **Internationally Accepted Credit Rating Agencies** Internationally accepted CRAs are recognized for bank supervisory purposes to undertake local and national ratings: *Provided*, That said CRAs shall have at least a representative office in the Philippines. Accordingly, credit ratings assigned by said CRAs may be used, among others, as basis for determining appropriate risk weights in ascertaining compliance with existing rules and regulations on risk-based capital requirements.

Sec. 4933Q ***(2008 - 4659Q.6)*** **Recognition of Fitch Singapore Pte Ltd as International Credit Rating Agency for Bank Supervisory Purposes.** The national or domestic credit ratings of Fitch Singapore Pte Ltd., a BSP-recognized international CRA with representative office in the Philippines, is hereby recognized by the BSP for bank supervisory purposes. Accordingly, national or domestic credit ratings assigned by Fitch Singapore Pte Ltd. may be used, among others, as basis for determining appropriate risk weights in ascertaining compliance with existing rules and regulations on risk-based capital requirements.

Secs. 4934Q - 4998Q (Reserved)

D. GENERAL PROVISION ON SANCTIONS

Sec. 4999Q (2008 - 4199Q) General Provision on Sanctions. Unless otherwise provided, any violation of the provisions of this Part shall be subject to Sections 36 and 37 of R.A. No. 7653.

The guidelines for the imposition of monetary penalty for violations/offenses with sanctions falling under Section 37 of R.A. No. 7653 on QBs, their directors and/or officers are shown in *Appendix Q-39*.

GUIDELINES TO EVALUATE INVESTMENT HOUSES
(Appendix to Sec. 4105Q)

a. *Capital* - The requirement is a minimum paid-in capital of ₱200.0 million for an investment house to be established in Metro Manila and ₱100.0 million for all others. Foreign equity, if any, shall be registered with and approved by the Board of Investments and the BSP.

b. *Citizenship* - Majority (51%) of the voting stock shall be owned by Filipinos.

c. *Directorship/Officership* - Majority of the board members shall be Filipinos. Resident foreign directors and technicians shall register with the Bureau of Immigration and Deportation. Compliance with the prohibition on interlocking directorship/officership between banks and investment houses and between QBs shall be observed.

d. *Promotion of Public Interest and Economic Growth* -

(1) Submission of a one (1)-year investment program indicating:

(a) *Underwriting and distribution activities*. These shall show in details the various stages leading to the completion of an agreement. Target dates for each stage in the underwriting process shall be indicated which should serve as reference points in the event that an investment house is unable to bring the program and its components to fruition. Target volume of underwriting would be set initially at twenty-five percent (25%) of paid-in capital.

(b) *Fund mobilization*. Emphasis shall be on maturities beyond one (1) year. Domestic and foreign sources shall be indicated and the latter shall be evaluated in terms of pertinent BSP regulations.

(c) *Fund usage*. Support of priority investment areas of the Government and other projects which may be determined by the BSP shall be emphasized. Funds placed on maturities beyond one (1) year shall be preferred.

(d) *Planned distribution of portfolio* Activities indicating money-market services and investment in subsidiaries and affiliates, while necessary to sustain the investment house, shall be subordinated to the preferred activities above-indicated. Other activities as financial management, counseling, distribution of equity and debentures for "public" ownership, etc., shall be considered.

(2) The one (1)-year investment program of the investment house shall be related to the government development plan by indicating the portion of the investment and savings targets in the plan which would be supported by the investment house industry.

(3) A one (1)-year projected income statement showing major sources of income and expense items.

(4) Operational agreement with other FIs.

(5) A statement justifying the operation of the investment house as not in conflict with public interest and economic growth, taking into account the existing number of investment houses, indicating:

(a) record of underwriting;

(b) evidence of medium and long-term loans;

(c) evidence of obtaining funds with maturity beyond one (1) year; and

(d) equity investments which were subsequently distributed to the public.

e. *Organization, Direction and Administration* - The organizational/ functional chart should match the organization framework with operational objectives. The management of the company, board of directors and the managerial staff, must be firmly designated before it can be granted a license to operate as an investment house.

f. *Integrity, Experience and Expertise of Board and Management Staff*

(1) Formal training, academic or others;

(2) Experience along financial management, securities dealing, fund management, project evaluation and feasibility studies;

(3) Absence of administrative or criminal conviction; and

(4) Affiliation with professional organizations.

g. *Branching* - The rate at which branch offices are to be established shall depend upon the ability of the company to conduct operations from headquarters/ head offices as well as on correspondent (banking) arrangements.

Other factors to be considered are the following:

(1) Reserve and liquidity position; and

(2) Profitability and capacity to absorb losses.

DETERMINATION OF AMOUNT OF ADDITIONAL CAPITAL THE ENTITY MUST PUT UP (PROJECTION BASE - LATEST AVAILABLE REPORT)

(in thousand pesos)

(Appendix to Subsec. 4151Q.2)

_____
(Name of Entity)

A.	1.	Estimated Amount of Risk Assets of Present Office for the Next 12 Months		
		a. Actual Risk Assets		₱ xxx
		b. Add: xx% of (a)		xxx
		Risk Assets - (Base Period)	₱ xxx	
		Risk Assets - (Previous Year)	xxx	
		Increase	₱ xxx	
		Rate of Increase = $\frac{\text{increase}}{\text{actual risk assets}}$ = xx%		
		c. Total of (a) and (b)		₱ xxx
	2.	Maximum Possible Level of Risk Assets Based on the Base Period Figures:		
		a. Net worth Less 30% of Paid-in Capital (₱xxx - xxx)	₱ xxx	
		b. 100% of Borrowings (Bills Payable)	xxx	
		c. 80% of Unutilized Acceptances or Credit Line with Foreign Bank(s)	xxx	₱ xxx
B.		Estimated Risk Assets for the First 12 Months of Operation:		
	1.	Branch Approved but not yet Opened:	₱ xxx	
	2.	Branch Being Applied for:	xxx	
		Add: Lower of A.1 or A.2	xxx	
C.		Total Estimated Risk Assets for 12 Months		₱ xxx
D.		10% of C (Minimum Paid-in Capital Required)		₱ xxx

E. Less:

Present Combined Capital Accounts (Base Period Figures)	₱ xxx	
Add: xx% of above	xxx	xxx
Capital Accounts - (Base Period)	₱ xxx	
Capital Accounts - (Previous Year)	xxx	
Increase	₱ xxx	

$$\text{*Rate of Increase} = \frac{\text{Increase}}{\text{Capital Accounts of Previous Year}} = xx\%$$

F. Estimated Excess of Capital over Minimum Capital Required or Additional Amount of Capital Applicant Must Put Up, as the case may be ₱ xxx

*The computation to arrive at the "rate of increase" in capital accounts shall only be considered if there is sufficient indication or evidence that the NBQB will continue to follow the same amount of increase in capital accounts for the succeeding year. If no evidence is found that the NBQB will continue to increase its capital accounts for the same amount for the succeeding year, then computations should consider only the amount of net profits (after dividends) plowed into the business for the year immediately preceding the date of application plus the amount of capital that the NBQB promised to put up per its schedule or program submitted to the Bangko Sentral. If no such schedule or program was submitted, then only the amount of net profits (after dividends) for the year immediately preceding the date of application should be considered.

LIST OF REPORTS REQUIRED FROM QUASI-BANKS

[Appendix to Sec. 4192Q (2008 - 4162Q)]

Category	Form No.	MOR Ref.	Report Title	Frequency	Submission Deadline	Submission Procedure
A-1	Unnumbered	4115Q *(Cir. No. 574 dated 07.10.07)*	Computation of the Adjusted Risk-Based Capital Adequacy Ratio Covering Combined Credit Risk, Market Risk and Operational Risk[1]	Quarterly		Original copy to CPCD/ISD
			- solo basis (Head Office and branches)		- 15th business day after end of reference quarter	
			- consolidated basis (Parent QB plus subsidiary financial allied undertakings but excluding insurance companies)		-30th business day after end of reference quarter	
A-2			Computation of the Risk-Based Capital Adequacy ratio Covering credit Risks	Quarterly		Appropriate department of the SES
			- solo basis (Head Office and branches)		- 15th business day after end of reference quarter	
			- consolidated basis (Parent QB plus subsidiary financial allied undertakings but excluding insurance companies)		-30th business day after end of reference quarter	
A-1		4192Q.3	Copy of Published Statement of Condition with Publisher's Certificate	Quarterly	5th business day from publication date	Original - Appropriate department of the SES
A-1	Unnumbered	4611Q.5 *(Cir.No. 668 dated 10.02.09)*	Report on Outstanding Derivatives Contracts	Monthly	15th banking day from end of reference month	-do-

[1] For QBs which are subsidiaries of UBs and KBs

Category	Form No.	MOR Ref.	Report Title	Frequency	Submission Deadline	Submission Procedure
A-1	Unnumbered	4611Q.5 *(Cir. No. 668 dated 10.02.09)*	Report on Trading Gains/(Losses) on Financial Derivatives	Monthly	15th banking day from end of reference month	Original - Appropriate department of the SES
A-2	Unnumbered (no prescribed form)	4141Q.9	Acknowledgment receipt of copies of specific duties and responsibilities of the board of directors and of a director and certification that they fully understand the same	Annual or as directors are elected	30th business day after date of election	Appropriate department of the SES
A-2	BSP-7-26-02-A/B	4192Q	Consolidated Statement of Condition *Schedules:*	Monthly	15th business day after end of reference month	Separate report for Head Office and each Branch; and a Consolidated Report for Head Office and Branches; to be submitted via electronic mail to SDC
A-2	BSP-7-26-02-A Schedule 1 (IHs only)	4192Q	Loans/Receivables, Trading Account Securities (TAS) - Loans Underwritten Debt Securities			
A-2	BSP-7-26-02-B Schedule 1 (FCs only)	4192Q	Loans/Receivables and Trading Account Securities (TAS) - Loans			
A-2	BSP-7-26-02-A Schedule 5 (For IHs)	4192Q	Bills Payable and Bonds Payable			
A-2	BSP 7-26-02-B Schedule 5 (For FCs)	4192Q	Bills Payable and Bonds Payable			
A-2	BSP-7-26-02-A/B Schedule 4	4192Q	Remaining Maturities of Selected Accounts Interest Rate and Maturity Matching			
A-2	BSP-7-26-02-A/B Schedule 3	4192Q	Interest Rate and Maturity Matching			

Category	Form No.	MOR Ref.	Report Title	Frequency	Submission Deadline	Submission Procedure
A-2	BSP-7-26-02-A Schedule 2 (For IHs)	4192Q	Underwritten Securities, Trading Account Securities - Investments, Available for Sale Securities and Investments in Bonds & Other Debt Instruments			
A-2	BSP-7-26-02-B Schedule 2 (For FCs)	4192Q	Trading Account Securities Investments, Available for Sale Securities and Investments in Bonds & Other Debt Instruments			
A-2	BSP-7-26-02-A Schedule 2.1 (For IHs)	4192Q	Underwritten Securities, Trading Account Securities - Investments, Available for Sale Securities and Investments in Bonds & Other Debt Instruments (Government Issue - Local Government Units)			
A-2	BSP-7-26-02-B Schedule 2.1 (For FCs)	4192Q	Trading Account Securities - Investments, Available for Sale Securities and Investments in Bonds & Other Debt Instruments (Government Issue - Local Government Units)			
A-2	BSP-7-26-02-A Schedule 1 (For IHs)	4192Q	Loans/Receivables, Trading Account Securities - Loans and Underwritten Debt Securities			
A-2	BSP-7-26-02-B Schedule 1 (For FCs)	4192Q	Loans/Receivables and Trading Account Securities - Loans			
A-2	BSP-7-26-02-B Schedule 1.1 (For FCs)	4192Q	Loans/Receivables and Trading Account Securities - Loans (Borrowing of Local Government Units)			
A-2	BSP-7-26-02-A Schedule 1.1 (For IHs)	4192Q	Loans/Receivables, Trading Account Securities - Loans and Underwritten Debt Securities (Borrowings of Local Government Units)			
A-2	BSP-7-26-02-B Schedule 6 (FCs only)	4192Q	Data on Firm's Businesses			

Category	Form No.	MOR Ref.	Report Title	Frequency	Submission Deadline	Submission Procedure
A-2	BSP-7-26-03-A/B	4192Q	Consolidated Statement of Income and Expenses	Monthly	15th business day following end of reference month	Separate report for Head Office and each branch; and a Consolidated Report for Head Office and Branches; to be submitted via electronic mail
A-2	BSP-7-26-05	4253Q *(As amended by MAB dated 02.24.05)*	Consolidated Report on Required and Available Reserves Against Deposit Substitutes and Special Financing	Weekly	4th business day following end of reference week	cc: mail or e-mail to SDC, hard copy to appropriate department of the SES
A-2	BSP-7-26-05.1	4253Q	Components of Deposit Substitutes with Original Maturities of 730 Days or Less	-do-	-do-	Separate report for Head Office and each branch; and a Consolidated Report for Head Office and Branches; to be submitted via electronic mail
	BSP-7-26-05.2	4253Q	Components of Deposit Substitutes with Original Maturities of more than 730 days			
A-2	BSB-7-26-05.3	4253Q	Eligible Philippine Government Securities Utilized as Reserves Against Deposit Substitutes	-do-	-do-	-do-
A-2	BSP-7-26-06	4115Q	Statement of Capital Required and Capital Accounts	Semi-Monthly	7th business day after 15th and end of month	E-mail to SDC: srsobqb@bsp.gov.ph
		4115Q	Control Prooflist duly signed by the authorized officer of the institution			Fax to SDC @ 523-3461

Category	Form No.	MOR Ref.	Report Title	Frequency	Submission Deadline	Submission Procedure
A-2	BSP-7-26-24	4192Q *(As amended by CL dated 08.06.03)*	Credit and Equity Exposures to Individuals/Companies/ Groups Aggregating P1 million and above.	Quarterly	15th business day from end of reference quarter	Electronic submission/ diskette - SDC
			Notarized Control Prooflist	-do-	-do-	Fax to SDC
A-2	Unnumbered (no prescribed form)	4239Q.3	Notice to BSP on SEC's approval of bond issue together with the documents required by the SEC for the creation and registration of the bond issue	As approved	3rd business day from approval by SEC	Original - Appropriate department of the SES
A-2	Unnumbered	4801Q *(Rev.May 2002 as amended by Cir. No. 612 dated 06.03.08)*	Report on Suspicious Transactions	As transaction occurs	10th business day from date of transaction/ knowledge	Original and duplicate - Anti-Money Laundering Council (AMLC)
A-2	Unnumbered	4801Q	Report on Covered Transactions	-do-	-do-	-do-
A-2	Unnumbered (no prescribed form)	4801Q	Certification of compliance with existing anti-money laundering regulations	Annually	20th business day after date of election	To be submitted to the appropriate department of the SES
A -2	Unnumbered	*(Cir. No. 609 dated 05.26.08 as amended by M-022 dated 06.26.08)*	Financial Reporting Package for Trust Institutions Schedules: Balance Sheet A1 to A2 Main Report B to B2 Details of Investments in Debt and Equity Securities	Quarterly	20th banking day after end of reference quarter	SDC sdcnbfi-frpti@bsp.gov.ph

Category	Form No.	MOR Ref.	Report Title	Frequency	Submission Deadline	Submission Procedure
			C to C2 Details of Loans and Receivables			
			D to D2 Wealth/Asset/Fund Management - UITF			
			E Fiduciary Accounts			
			E1 to E1B Other Fiducirary Services - UITF			
			Income Statement			
			Control Prooflist	Quarterly	20th banking day after end of reference quarter	SDC sdcnbfi-frpti@bsp.gov.ph
A-3	BSP-7-26-18DF	4326Q	Consolidated Monthly Report on Credit Accommodations to Directors, Officers, Stockholders and Their Related Interests	Monthly	15th calendar day from end of reference month	SDC
A-3	BSP-7-26-18.1	4326Q	Credit Accommodations to Directors, Officers, Stockholders, and Their Related Interests	-do-	-do-	Original CPCD/ISD
A-3	Unnumbered	4192Q *(CL-050 dated 10.04.07 and CL-059 dated 11.28.07)*	Report on Borrowings of BSP Personnel	Quarterly	15th business day after end of reference quarter	Original to SDC
A-3	Unnumbered	4334Q	Copy of Written Approval of Board of Directors on Credit Accommodations to Directors, Officers, Stockholders, and Their Related Interests	As Approved	20th business day from date of approval	Original - Appropriate department of the SES
A-3	Unnumbered	4328Q.5 *(Cir. No. 560 dated 01.31.07)*	Transmittal of Board Resolution/Written Approval on Credit Accomodations to Subsidiaries and/or Affiliates	As loan to subsidiaries and/or affiliates is approved	20th banking day after date of approval or director	Original and duplicate appropriate department of the SES

Category	Form No.	MOR Ref.	Report Title	Frequency	Submission Deadline	Submission Procedure
B	Unnumbered	4141Q.4	Notice of Election/Appointment of Members of Board of Directors and Committees	As change occurs	10th day from election/ assumption of office	Original - Appropriate department of the SES
B	Unnumbered (no prescribed form)	4143Q.4	Report on Disqualification of Director/Officer	As disqualification occurs	Within 72 hours from receipt of report by board of directors	Appropriate department of the SES
B	BSP-7-26-13	4306Q	Past Due Receivables, Loans and/or Commercial Papers/Private Securities	Quarterly	15th calendar day after end of reference quarter	Original - Appropriate department of the SES
B	BSP-7-26-15 (IH only)	4192Q	Report on Underwriting Activities	-do-	End of month following each quarter	-do-
B	BSP-7-26-20	4381Q	Report on Equity Investments in Non-Allied Undertakings	Semestrally	15th business day following end of reference semester	-do-
B	BSP-7-26-21	4103Q *(As amended by Cir. No. 557 dated 01.12.07)*	Borrowing-Investment Program	Annually	on or before Nov. 30	See Annex Q-3-a for details of the report
B	BSP-7-26-22 (IH only)	4192Q	Annual Underwriting Program	Annually	1st working day of March of reference year	Original - Appropriate department of the SES
B	BSP-7-26-26	4192Q.3	Statement of Condition for Publication (See Sec. 4192Q.3 for requirement on publication of names of directors/officers) Control Prooflist duly signed by the authorized officer of the institution	Quarterly	20th business day from receipt of call	E-mail to SDC: srso-nbqb@ bsp.gov.ph Fax to SDC@ 523-3461

Category	Form No.	MOR Ref.	Report Title	Frequency	Submission Deadline	Submission Procedure
B	Unnumbered	4235Q.14	Daily Report on Interbank Borrowings not Effected Through Clearing Account with BSP	Daily (only when there are transactions covered)	Noon of business day following date of report	Original - Appropriate department of the SES
B	Unnumbered	4190Q	Consolidated Annual Financial Statements of Financial Intermediaries and their Allied Undertakings/Affiliates/Subsidiaries supported by Individual Annual Undertakings/Affiliates/Subsidiaries and their Audited Financial Statements (Refer to Subsec. 4192Q.3 for guidelines on consolidation of statements)	Annually	120th calendar day after end of reference year	-do-
B	Unnumbered (no prescribed form)	4192Q	Annual Report of Management to Stockholders Covering Results of Operations for the Previous Year	Annually	As soon as available	-do
B	Unnumbered (no prescribed form)	4190Q	Audited Financial Statements for Previous Year Prepared by the External Auditor and the Corresponding Auditor's Letter of Comments	Annually	90th day after the start of audit	-do-
B	Unnumbered	4192Q	Report on Crimes/Losses for Head Office/Branches See Annex Q-3-c for reporting guidelines	As crime or incident occurs	48th hour from knowledge of crime/ incident	-do-
B	Unnumbered	4192Q	Board resolution on quasi-bank's signatories of report submitted to BSP	As authorized	3rd day from date of resolution	-do-
B	Unnumbered	4192Q	Documentary requirements/information on organizational structure and operational policies	Upon submission of application to engage in QBF		See Annex Q-3-e for documentary requirements/information required
				As changes occurs	15th calendar day from change/issuance	-do-

Category	Form No.	MOR Ref.	Report Title	Frequency	Submission Deadline	Submission Procedure
B	Unnumbered (no prescribed form)	4192Q	Corporate Secretary's Certification under oath on list of stockholders and/or groups of stockholders	As change in composition of stockholders occurs	Immediately after change	Original - Appropriate department of the SES
B	Unnumbered (no prescribed form)	4425Q.2	Report on Required and Available Reserves on Peso-Denominated CTFs, Such Other Managed Peso Funds and TOFA-Others	Weekly	3rd business day following reference week	To be submitted by institutions with trust operations
						Original - Appropriate department of the SES
			Control Prooflist duly signed by the authorized officer of the institution			E-mail to SDC: srso-nbqb@bsp.gov.ph
						Fax to SDC @ 523-3461
			Reconciliation statement on demand deposit with BSP	Monthly	7th business day from receipt of BSP statement of account	Original to be submitted to BSP Comptrollership Department; one copy to appropriate department of the SES
B	Unnumbered	4625Q.9 *(Rev. Dec. 2007 per Cir. No. 591 dated 12.27.07)*	Report on FX Swaps with Customers[1] where 1st Leg is a Purchase of FX Against Pesos (For QBs with derivatives license	Monthly	5th business day after end of reference month	ID @ e-mail: iod@bsp.gov.ph cc: mail SDC
B	Unnumbered	4625Q.9	Report on Cancellations, Roll-overs and Non-Delivery of FX Forwards Purchase-Sales Contracts and Forward Leg of Swap Contracts[1] (For QBs with derivatives license)	Monthly	5th business day after end of reference month	-do-

Category	Form No.	MOR Ref.	Report Title	Frequency	Submission Deadline	Submission Procedure
B	SES Form 6H (CBP-7-16-21), revised	4306Q.5	Notice/Application for Write-off of Loans, Other Credit Accommodations, Advances and Other Assets	As write-off occurs	25th business day prior to the intended date of write-off	Original and duplicate - Appropriate department of the SES
			Waiver of the Confidentiality of Information under Sections 2 and 3 of R.A. No. 1405, as amended	As transaction occurs		
B	SEC Form	*MAB dated 09.02.05*	General Information Sheet	Annually	30th day from date of Annual Stockholders' meeting or if changes occur, 7th day from date of change	Drop box - SEC Central Receiving Section
		M-005 dated 02.04.08	Disclosure Statement on SPV Transactions	Quarterly	15th banking day after end of reference quarter	SDC
		M-019 dated 05.05.08	Report on NDF transactions wirh non-resident	Weekly	2nd banking day after end of reference week	Email to SDC sdc-ndf@bsp.gov.ph cc: Treasury Dept. fx-omo@bsp.gov.ph
			Control Prooflist			Fax to SDC @ (632) 5233461 or 5230230
B	Unnumbered	4235Q.12 *(Cir. No. 467 dated 01.10.05)*	Report on the Undocumented Repurchase Agreements	-do-	Within 72 hours from knowledge of transactions	Appropriate department of the SES

Category	Form No.	MOR Ref.	Report Title	Frequency	Submission Deadline	Submission Procedure
B	Unnumbered	4235Q.12 *(Cir. No. 467 dated 01.10.05)*	Notarized certification that the bank did not enter in Repurchase Agreement covering Government Securities, Commercial Papers and other Non-Negotiable Securities or Instruments that are not documented	Semestral	5th banking day after end of every semester	Appropriate department of the SES
B	SES II Form 15 (NP08-TB)	4142Q *(As amended by M-024 dated 07.31.08)*	Biographical Data of Directors/Officers - If submitted in diskette form - Notarized first page of each of the directors'/officers' bio-data saved in diskette and control prooflist - If sent by electronic mail - Notarized first page of Biographical Data or Notarized list of names of Directors/Officers whose Biographical Data were submitted thru electronic mail to be faxed to SDC (CL dated 01.09.01)	After election or appointment and as changes occur	7th banking day from the date of the meeting of the board of directors in which the directors/ officers are elected or appointed	Email to SDC or hardcopy - Appropriate department of the SES cc: SDC
		MAB dated 09.02.05	Certification under oath of independent directors that he/she is an independent directors as defined under Subsec. X141.10 and that all the information thereby supplied are true and correct			
		Cir. No. 513 dated 02.10.06	Verified statement of directors/officers that he/she has all the aforesaid qualifications and none of the disqualifications			
B	Form 1 Schedule 1	*M-031 dated 09.11.09 and Cir. No. 649 dated 03.09.09*	Report on Electronic Money Transactions Quarterly Statement of E-Money Balances and Activity - Volume and Amount of E-Money Transactions Schedule 1 - E-Money Balances	Quarterly	15 banking day after end of reference quarter	e-mail - sdcnbfiemoney@bsp.gov.ph hardcopy - SDC

Annex Q-3-a

INFORMATION ON ONE-YEAR BORROWING-INVESTMENT PROGRAM TO BE SUBMITTED BY QUASI BANKS

(Annex to Appendix Q-3)

1. Investment areas indicating industry direction of the corporation engaged in quasi-banking, indicating as a minimum, the following:

(a) money market operations;
(b) investments in stocks and bonds;
(c) investments in government securities;
(d) receivables financing;
(e) leasing activities; and
(f) direct loaning operations.

Likewise to be disclosed are the other preferred areas of investment, e.g., real estate, condominium, and those related to the government programs and other projects which may be determined by the BSP.

For investment houses with quasi-banking functions, the proposed underwriting program, as well as the previous year's activities, shall also be submitted identifying debt and equity issues.

2. Borrowing operations to support the investment program indicating among others:

(a) Maturity - short-term: less than a year
- medium-term: one (1) year to five (5) years
- long-term: more than five (5) years

(b) Interest rate per annum for the above three types of borrowings (more indicatory than fixed).

Individual or institutional source of funds; whether domestic or foreign, governmental or private, financial or non-financial.

3. Preference shall be given to fund usage and mobilization at terms beyond one (1) year.

Annex Q-3-b

GUIDELINES GOVERNING THE CONSOLIDATION OF FINANCIAL STATEMENTS OF FINANCIAL INTERMEDIARIES AND THEIR ALLIED UNDERTAKINGS/SUBSIDIARIES/AFFILIATES

(Annex to Appendix Q-3)

(deleted by Cir. No. 494 dated 20 September 2005)

Annex Q-3-c

REPORTING GUIDELINES ON CRIMES/LOSSES

(Annex to Appendix Q-3)

1. QBs shall report on the following matters through the appropriate department of the SES:

a. Crimes whether consummated, frustrated or attempted against property/ facilities (such as robbery, theft, swindling or estafa, forgery and other deceits) and other crimes involving loss/destruction of property of the QBs when the amount involved in each crime is ₱20,000 or more.

Crimes involving QB personnel, regardless of whether or not such crimes involve the loss/destruction of property of the QB, even if the amount involved is less than those above specified, shall likewise be reported to the BSP.

b. Incidents involving material loss, destruction or damage to the institution's properties/facilities, other than arising from a crime, when the amount involved per incident is ₱100,000 or more.

2. The following guidelines shall be observed in the preparation and submission of the report.

a. The report shall be prepared in two (2) copies and shall be submitted within five (5) business days from knowledge of the crime or incident, the original to the appropriate department of the SES and the duplicate to the BSP Security Coordinator, thru the Director, Security Investigation and Transport Department.

b. Where a thorough investigation and evaluation of facts is necessary to complete the report, an initial report submitted within the five (5)-business day deadline may be accepted: *Provided*, That a complete report is submitted not later than fifteen (15) business days from termination of investigation.

Annex Q-3-d

DOCUMENTARY REQUIREMENTS ON DIRECTORS/OFFICERS/ MAJOR INDIVIDUAL STOCKHOLDERS

(Annex to Appendix Q-3)

(Deleted by Circular No. 661 dated 01 September 2009)

Annex Q-3-e

DOCUMENTS/INFORMATION ON ORGANIZATIONAL STRUCTURE AND OPERATIONAL POLICIES

(Annex to Appendix Q-3)

I. *Documents on organizational structure and operational policies*

1. Chart of the firm's organizational structure or any substitute therefor;

2. Name of departments/units/offices with their respective duties and responsibilities;

3. Designations of positions in each department/unit/office with the respective duties and responsibilities;

4. Manual of Instructions or the like embodying the operating policies/ procedures of each department/unit/office, covering such areas as:

(a) Signing/delegated authority;

(b) Procedure/flow of paper work; and

(c) Other matters.

5. Memoranda-Circulars or the like issued covering organizational and operational and operation policies;

6. Sample copies of each of the forms/reports used by each office/unit/ department other than those submitted to the BSP; and

7. Such other documents/information which may be required from time to time.

II. *Other Data*

1. Name of Institution

2. Address

3. P.O. Box number

5. Board of Directors including Corporate Secretary:

(a) Names of Chairman, Vice-Chairman and Directors

(b) Number of directors per By-Laws

(c) Number of vacancies in the Board

(d) Names of corporations where they serve as Chairman of the Board or as President and names of other business enterprises of which they are proprietors or partners

(e) For the Corporate Secretary, indicate if he is also a Director

(f) Date of annual election of directors per By-Laws

6. Executive officers including Auditor:

(a) Names and titles

(b) Telephone number of each officer (office)

(c) For the Executive Vice-President, state the names of corporations where he serves as Chairman of the Board and names of other business enterprises where he is proprietor or partner

(d) For Vice-Presidents and other officers with non-descriptive titles, indicate area of responsibility, e.g. Vice-President for Operations or Vice-President, International Department

(e) Include officers from President to Vice-President

7. Branches, agencies and extension offices:

(a) Name of branch, agency or extension office, e.g. Quiapo Branch or Makati Agency

(b) Address

(c) Names and telephone number of:

(1) Manager

(2) Cashier

(3) Accountant

(d) For agencies and extension offices, indicate name of mother branch.

Annex Q-3-f

GUIDELINES ON CALCULATING ADDITIONAL INFORMATION REQUIRED IN PUBLISHED STATEMENT OF CONDITION

(*Annex to Appendix Q-3)*

In calculating the additional information required to be disclosed in the Statement of Condition for publication, the following guidelines shall be observed:

1. All amounts and ratios to be reported shall be as of the same call date. However, the basis for computing the Return on Average Equity shall be the latest quarter immediately preceding the call date.

2. Return on Average Equity shall be computed as follows:

$$\text{Return on Average Equity (\%)} = \frac{\text{Net Income/(Loss) After Income Tax}}{\text{Average Total Capital Accounts}} \times 100$$

Where Net Income After Tax and Average Total Capital Accounts shall be:

	Net Income After Tax	Average Total Capital Accounts
March	Quarter End Net Income After Tax Multiplied by 4	Sum of end-month Capital Accounts (December-March) divided by 4.
June	Semester End Net Income After Tax Multiplied by 2	Sum of end-month Capital Accounts (December - June) divided by 7.
September	Nine (9) months Ended Net Income After Tax multiplied by 1.333333	Sum of end-month Capital Accounts (December – September) divided by 10.
December	Year Ended Net Income After Tax	Sum of end-month Capital Accounts (December - December) divided by 13.

GUIDELINES ON PRESCRIBED REPORTS SIGNATORIES AND SIGNATORY AUTHORIZATION

[Appendix to Subsec. 4192Q.1 (2008 - 4162Q.1)]

Category A-1 reports shall be signed by the chief executive officer, or in his absence, by the executive vice president, and by the comptroller, or in his absence, by the chief accountant, or by officers holding equivalent positions. The designated signatories in this category, including their specimen signatures, shall be contained in a resolution approved by the board of directors in the format prescribed in Annex Q-4-a.

Category A-2 reports of head offices shall be signed by the president, executive vice-presidents, vice-presidents or officers holding equivalent positions. Such reports of other offices/units (such as branches) shall be signed by their respective managers/officers in-charge. Likewise, the signing authority in this category shall be contained in a resolution approved by the board of directors in the format prescribed in Annex Q-4-b.

Categories A-3 and B reports shall be signed by officers or their alternates, who shall be duly designated in a resolution approved by the board of directors in the format as prescribed in Annex Q-4-c.

Copies of the board resolutions on the report signatory designations shall be submitted to the appropriate department of the SES within three (3) days from the date of resolution.

Annex Q-4-a

FORMAT OF RESOLUTION FOR SIGNATORIES OF CATEGORY A-1 REPORTS

Resolution No. _____

Whereas, it is required under Subsec. 4192Q.1 that Category A-1 reports be signed by the Chief Executive Officer, or in his absence, by the Executive Vice-President, and by the comptroller, or in his absence, by the Chief Accountant, or by officers holding equivalent positions.

Whereas, it is also required that aforesaid officers of the institution be authorized under a resolution duly approved by the institution's Board of Directors;

Whereas, we, the members of the Board of Directors of ___(Name of Institution)___, are conscious that, in designating the officials who would sign said Category A-1 reports, we are actually empowering and authorizing said officers to represent and act for or in behalf of the Board of Directors in particular and _____(Name of Institution)_____ in general;

Whereas, this Board has full faith and confidence in the institution's Chief Executive Officer, Executive Vice-President, Comptroller and Chief Accountant, as the case may be, and, therefore, assumes responsibility for all the acts which may be performed by aforesaid officers under their delegated authority;

Now, therefore, we, the members of the Board of Directors, resolve, as it is hereby resolved that:

1. Mr._____	President	_____ Specimen Signature
	or	
	Executive	
2. Mr._____	Vice-President	_____ Specimen Signature
	and	
3. Mr._____	Comptroller	_____ Specimen Signature
	or	
	Chief	
4. Mr._____	Accountant	_____ Specimen Signature

are hereby authorized to sign Category A-1 reports of ____(Name of Institution)____.

Done in the City of _____ Philippines, this ____day of ____, 20____.

_____
CHAIRMAN OF THE BOARD

_____ DIRECTOR	_____ DIRECTOR
_____ DIRECTOR	_____ DIRECTOR
_____ DIRECTOR	_____ DIRECTOR

ATTESTED BY:

_____
CORPORATE SECRETARY

Annex Q-4-b

FORMAT OF RESOLUTION FOR SIGNATORIES OF CATEGORY A-2 REPORTS

Resolution No. _____

Whereas, it is required under Subsec. 4192Q.1 that Category A-2 reports of head offices be signed by the President, Executive Vice-Presidents, Vice-Presidents or officers holding equivalent positions, and that such reports of other offices be signed by the respective managers/officers-in-charge;

Whereas, it is also required that aforesaid officers of the institution be authorized under a resolution duly approved by the institution's Board of Directors;

Whereas, we, the members of the Board of Directors of __(Name of Institution)___, are conscious that, in designating the officials who would sign said Category A-2 reports, we are actually empowering and authorizing said officers to represent and act for or in behalf of the Board of Directors in particular and __(Name of Institution)__ in general;

Whereas, this Board has full faith and confidence in the institution's President (and/or the Executive Vice-President, etc., as the case may be) and, therefore, assumes responsibility for all the acts which may be performed by aforesaid officers under their delegated authority;

Now, therefore, we, the members of the Board of Directors, resolve, as it is hereby resolved that:

Name of Officer	*Specimen Signature*	*Position Title*	*Report No.*
_____	_____	_____	_____

are hereby authorized to sign the Category A-2 reports of ____(Name of Institution)____.

Done in the City of _____ Philippines, this ____day of ____, 20____.

_____
CHAIRMAN OF THE BOARD

_____ _____
DIRECTOR DIRECTOR

_____ _____
DIRECTOR DIRECTOR

_____ _____
DIRECTOR DIRECTOR

ATTESTED BY:

_____
CORPORATE SECRETARY

Annex Q-4-c

FORMAT OF RESOLUTION FOR SIGNATORIES OF CATEGORIES A-3 AND B REPORTS

Resolution No. _____

Whereas, it is required under Subsec. 4192Q.1 that Categories A-3 and B reports be signed by officers or their alternates;

Whereas, it is also required that aforesaid officers of the institution be authorized under a resolution duly approved by the institution's Board of Directors;

Whereas, we the members of the Board of Directors of __(Name of Institution)__ are conscious that, in designating the officials who would sign said Categories A-3 and B reports, we are actually empowering and authorizing said officers to represent and act for or in behalf of the Board of Directors in particular and __(Name of Institution)__ in general;

Whereas, this Board has full faith and confidence in the institution's authorized signatories and, therefore, assumes responsibility for all the acts which may be performed by aforesaid officers under their delegated authority;

Now, therefore, we, the members of the Board of Directors, resolve, as it is hereby resolved that:

Name of Authorized Signatory/Alternate	Specimen Signature	Position Title	Report No.
1. Authorized			
(Alternate)			
2. Authorized			
(Alternate)			
etc.			

are hereby authorized to sign the Category A-3 and B reports of __(Name of Institution)__.

Done in the City of _____ Philippines, this ____day of ____, 20____.

_____
CHAIRMAN OF THE BOARD

_____ _____
DIRECTOR DIRECTOR

_____ _____
DIRECTOR DIRECTOR

ATTESTED BY:

_____
CORPORATE SECRETARY

MINIMUM INTERNAL CONTROL STANDARDS FOR QUASI-BANKS

(Appendix to Sec. 4185Q (2008 - 4171Q)]

I. Proper Accounting Records

1. QBs should maintain proper and adequate accounting records.

2. These records should be kept currently posted and should contain sufficient detail so that an audit trail is established.

3. All entries should bear official approval and should be initialed by the person originating and another person checking them.

II. Independent Balancing

1. Independent balancing shall mean that records posted by a person or cash held by a cashier shall be balanced or counted by another person.

2. The minimum independent balancing procedures which should be adopted are the following:

a. Monthly reconcilement of general ledger balances against their respective subsidiary and supporting records and documentations by someone other than the bookkeeper, the person handling the records, or the person directly connected with processing the transactions.

b. Irregular and unannounced count of cashier's cash and checks and other cash items at least twice a month by the auditor/ control officer or by an officer not connected with the treasurer's/cashier's office or its equivalent.

c. Monthly reconcilement of cash in banks accounts (domestic and foreign) and due from/to head office/branches by someone other than the check custodian, the person posting the general ledger entries or the authorized signatory of the bank account.

d. Periodic verification of securities and collaterals by someone other than their custodians. Verification should include both the physical inventory of securities and the record checking.

e. Periodic verification of the accuracy of the interest credits and payments to deposit substitute liabilities accounts.

3. All exceptions in the reconciliation/ verification should be followed up immediately until satisfactorily corrected.

III. Division of Duties and Responsibilities

1. The duties of all the officers and employees should be segregated, clearly defined, understood, documented and manualized if possible. No individual shall have complete authority and responsibility for handling all phases of any transaction from beginning to end.

2. The physical handling of a transaction should be separated from its recording and supervision as follows:

a. A person handling cash should not be permitted to post the ledger records nor should posting of the general ledger be performed by an employee who posts the investor's/creditor's subsidiary ledgers;

b. A loaning officer should never be allowed to disburse proceeds of notes, accept note payment nor process loan ledgers;

c. The functions of issuing, recording and signing of checks should be separated;

d. The receipt of statements from depository banks should be assigned to an employee other than the one connected with the preparation, recording and signing of checks;

e. Custodians of securities should not be allowed to handle security transactions;

f. Collateral appraisals should be done by an employee/officer other than the ones approving the loans;

g. Incoming checks and other cash items should be recorded chronologically in a register by an employee other than the bookkeeper;

h. Credit reports should be obtained by someone other than lending officers;

i. Mailing of client's statements and delinquent notices should be done by an employee other than the one who granted the loan or the one handling the records; and

j. Paid checks/drafts should be controlled and maintained by an officer/ employee other than the authorized signatory or the cashier.

3. Extensive background checking of persons intended to be assigned to handle cash and securities should be conducted. Frequent follow-up checking after their employment should also be made.

IV. Joint Custody

1. Joint custody shall mean the processing of transactions in the presence of and under the direct observation of a second person. Both persons shall be equally accountable for the physical protection of the items and records involved.

2. Physical protection should be deemed established through the use of two (2) locks or combinations on a file chest or vault compartment.

3. Two (2) or more persons should be assigned to each half of the control so that operating efficiency is not impaired if one person is not immediately available.

4. Persons who are related to each other within the third degree of consanguinity or affinity should not be made joint custodians.

5. The following should be under joint custody:

a. Cash on hand or in vault
b. All accountable forms
c. Collaterals
d. Securities
e. Documents of title and/or ownership of properties or fixed assets
f. Safekeeping items
g. Vault doors and safe combinations.

V. Signing Authorities

Signing authorities for the different levels of officers to sign for and in behalf of the institutions should be approved by the board of directors and the extent of each level of authority should be clearly defined. These signing authorities should include but need not be limited to the following:

a. Lending;
b. Borrowing;
c. Investments;
d. Approval of expenses;
e. Various supervisory reports; and
f. Checks.

VI. Dual Control

1. Dual control shall mean the work of one (1) person is to be verified by a second person to determine (a) that proper authority has been given to handle the transaction, (b) that the transaction is properly recorded, and (c) that proper settlement of the transaction is made.

2. The routine of each transaction should be designed so that at least two (2) or more individuals are involved in the completion of every transaction.

3. The following accounts/transactions should be under dual control:

a. Checks - The signature of at least two (2) officers should be required in the issuance of checks.

b. Borrowing - The signature of at least two (2) authorized officers should be required.

c. All transactions giving rise to "due to" or "due from" account and all instruments of remittances evidencing

these transactions particularly those involving substantial amounts, should be approved by two (2) authorized officers.

VII. Number Control

1. Sequence number controls should be incorporated in the accounting systems and should be used in registering notes, in issuing official checks and in other similar situations. Number control should be policed by a person designated by senior management who should be detached from the particular operations involved.

2. The following are the forms, instruments and accounts that should be number-controlled:

a. Checks;

b. Promissory notes and other commercial papers;

c. Official and provisional receipts;

d. Certificate of stocks;

e. Loan accounts; and

f. Expense vouchers.

VIII. Rotation of Duties

1. The duties of personnel handling cash, securities and bookkeeping records should be rotated.

2. Rotation assignment should be irregular, unannounced and long enough to permit disclosure of irregularities or manipulations.

IX. Independence of the Internal Auditor

1. The position of internal auditor should be provided for in the by-laws together with the duties and responsibilities, scope and objectives of internal auditing.

2. The internal auditor should report directly to the Audit Committee.

3. The internal auditor should not install nor develop procedures, prepare records or engage in other activities which he normally reviews or appraises.

X. Direct Verification

1. Direct verification shall mean the confirmation of account or records by direct correspondence/visits with the institution's customers.

2. The following accounts, among others, should be subject to direct verification by the internal auditing staff at least once a year:

a. Balances of loans and credit accommodations of borrowers;

b. Outstanding balances of borrowings and other liabilities;

c. Outstanding balances of receivables/ payables; and

d. Collaterals securing said accounts.

XI. Other Internal Control Standards

1. Investments

a. Investment limits and a list of accredited companies as approved by the Board of Directors or by its Credit Committee should be established as a guide for investing in any FI engaged in money market trading.

b. Investments should be secured by assets approved by the Board of Directors or by its Credit Committee.

c. Checks representing placements of investments should be released only upon receipt of either the deposit substitute instrument or the underlying securities or documents of title.

2. Miscellaneous

a. Loan applications and related documents should be spot-checked to insure their authenticity, including verification of name, residence, employment and current reputation of the borrowers.

b. No employee should be permitted to process transaction affecting his own account.

c. Cashiers and other employees having contact with customers should be prohibited from preparing deposit substitute tickets or other records for the customers.

d. QBs should have a sound recruitment policy since internal control begins from point of hiring.

e. QBs should secure adequate insurance coverages, fidelity and other indemnity protection, viz:

(1) Insurance coverage - for losses arising from calamities and theft/ robberies.

(2) Fidelity bonds - for losses arising from dishonest, fraudulent and criminal acts of accountable officers/employees.

STANDARDIZED DEPOSIT SUBSTITUTE INSTRUMENTS

[Appendix to Subsec. 4235Q.3 (2008 - 4211Q.3)]

Serial No._____

_____
(Name of Quasi-Bank)

PROMISSORY NOTE

Issue Date : _____ , 20____
Maturity Date : _____ , 20____

FOR PESOS _____ (₱_____)
(Present Value/Principal)

RECEIVED, _____ promises to pay
(Name of Issuer/Maker)

_____ or order, the sum
(Name/Account Number of Payee)

of PESOS _____ (₱_____)
(Maturity Value/Principal & Interest)

subject to the terms and conditions on the reverse side hereof.

_____
(Duly Authorized Officer)

NOT INSURED WITH THE PHILIPPINE DEPOSIT INSURANCE CORPORATION (PDIC)

APP. Q-6
08.12.31

TERMS AND CONDITIONS OF A PROMISSORY NOTE

1. ***Computation of Yield***
   Interest is hereby stipulated/computed at_____% per annum, compounded
   ( ) monthly ( ) quarterly ( ) semi-annually ( ) others.

2. ***No Pretermination***
   This promissory note shall not be honored or paid by the issuer/maker before the maturity date indicated on the face hereof.

3. ***Liquidated Damages***
   In case of default, issuer/maker shall pay, in addition to stipulated interest, liquidated damages of _____ (Amount or %) _____, plus attorney's fees of _____ (Amount or %) _____ and costs of collection in case of suit.

4. ***Renewal***
   ( ) No automatic renewal.
   ( ) Automatic renewal under the following terms:

   _____

   _____

5. ***Collateral/Delivery***
   ( ) No collateral
   ( ) Collateral/secured by _____ (describe collateral) _____
   ( ) Physically delivered to Payee
   ( ) Evidenced by Custodian Receipt No. _____ dated _____ issued _____ by _____
   ( ) Collateralized/secured by _____ (fraction or %) _____ share of _____ (describe collateral) _____ as evidenced by Custodian Receipt No. _____ dated _____ issued by _____ .

6. ***Substitution of Securities***
   ( ) Not acceptable to Payee
   ( ) Acceptable to Payee, however, actual substitution shall be with prior written consent of payee.

7. ***Separate Stipulations***
   ( ) This Agreement is subject to the terms and conditions of _____ (describe document) _____ dated _____ executed by _____ (name of party/ies) _____ and made an integral part hereof.

Serial No._____

_____
(Name of Quasi-Bank)

REPURCHASE AGREEMENT

Issue Date : _____ , 20___
Repurchase Date : _____ , 20___

FOR AND IN CONSIDERATION OF PESOS _____(₱ _____)
Vendor, (name of Quasi-Bank) hereby sells, transfers and conveys in favor of Vendee, (name of Vendee) the security(ies) described below, it being mutually agreed upon that the same shall be resold by Vendee and repurchased by Vendor on the repurchase date indicated above at the price of PESOS _____(₱_____), subject to the terms and conditions stated on the reverse side hereof.

(Description of Securities)

Issuer	Serial Number/s	Maturity Date/s	Face Value	Interest/Yield
			₱	₱
		TOTAL	₱	₱

CONFORME:

_____
(Duly Authorized Officer)

_____
(Signature of Vendee)

NOT INSURED WITH THE PHILIPPINE DEPOSIT INSURANCE CORPORATION (PDIC)

APP. Q-6
08.12.31

TERMS AND CONDITIONS OF A REPURCHASE AGREEMENT

1. ***Computation of Yield***
   Yield is hereby stipulated/computed at ____% per annum, compounded
   ( ) monthly ( ) quarterly ( ) semi-annually ( ) others.

2. ***No Pretermination***
   Vendor shall not repurchase subject security/ies before the repurchase date stipulated on the face of this document.

3. ***Liquidated Damages***
   In case of default, the Vendor shall be liable, in addition to stipulated yield, for liquidated damages of _____(Amount or %)_____ , plus attorney's fees of_____(Amount or %)_____, and costs of collection in case of suit.

4. ***Renewal***
   ( ) No automatic renewal
   ( ) Automatic renewal under the following terms:

   _____

   _____

5. ***Delivery/Custody of Securities***
   ( ) Physically delivered to Payee
   ( ) Evidenced by Custodian Receipt No. _____ dated,_____
   issued by_____

6. ***Substitution of Securities***
   ( ) Not acceptable to Payee
   ( ) Acceptable to Payee, however, actual substitution shall be with prior written consent of payee.

7. ***Separate Stipulations***
   ( ) This Agreement is subject to the terms and conditions of__(describe document)__
   dated_____ , executed by_____(name of Party/ies)_____
   and made an integral part hereof.

Serial No. _____

_____
(Name of Quasi-Bank)

CERTIFICATE OF ASSIGNMENT WITH RECOURSE

Issue Date: _____, 20 _____

FOR AND IN CONSIDERATION OF PESOS _____(P _____)
_____(name of Assignor)_____ hereby assigns, conveys, and transfers with recourse to _____(name of Assignee)_____ the debt of (name of Principal Debtor) to the Assignor, specifically described as follows:

(Description of Debt Securities)

Principal Debtor	Serial Number/s	Maturity Date/s	Face Value	Interest/Yield
			₱	₱
		TOTAL	₱	₱

and Assignor hereby undertakes to pay, jointly and severally with the Principal Debtor, the face value of, and the interest/yield on, said debt securities. The assignment shall be subject to the terms and conditions on the reverse side hereof.

C O N F O R M E :

_____
(Duly Authorized Officer)

_____
(Signature of Assignee)

NOT INSURED WITH THE PHILIPPINE DEPOSIT INSURANCE CORPORATION (PDIC)

APP. Q-6
08.12.31

TERMS AND CONDITIONS OF CERTIFICATE OF ASSIGNMENT WITH RECOURSE

1. ***No Pretermination***
   Assignor shall not pay nor repurchase subject security/ies before the maturity date thereof.

2. ***Liquidated Damages***
   In case of default, Assignor shall be liable, in addition to interest, for liquidated damages of (Amount or %) plus attorney's fees of (Amount or %), and costs of collection in case of suit.

3. ***Delivery/Custody of Securities***
   ( ) Physically delivered to Assignee
   ( ) Evidenced by Custodian Receipt No. _____ dated _____, issued by _____.

4. ***Separate Stipulations***
   ( ) This Agreement is subject to the terms and conditions of _____, dated _____ executed by (name of Party/ies) and made an integral part hereof.

Serial No. _____

_____
(Name of Quasi-Bank)

CERTIFICATE OF ASSIGNMENT WITH RECOURSE

Issue Date: _____ , 20____

FOR AND IN CONSIDERATION OF PESOS (Present Value/Principal) (₱____), (name of Assignor) hereby assigns, conveys, and transfers with recourse to (name of Assignee) the debt of (name of Principal Debtor) to the Assignor, specifically described as follows:

Principal Debtor	Serial Number/s	Maturity Date/s	Face Value	Interest/Yield
			₱	₱
		TOTAL	₱	₱

and hereby undertakes that in case of default of the Principal Debtor, Assignor shall pay the face value of, and the interest/yield on, said debt securities, subject to the terms and conditions on the reverse side hereof.

CONFORME:

_____
(Duly Authorized Officer)

_____
(Signature of Assignee)

NOT INSURED WITH THE PHILIPPINE DEPOSIT INSURANCE CORPORATION (PDIC)

APP. Q-6
08.12.31

TERMS AND CONDITIONS OF CERTIFICATE OF ASSIGNMENT WITH RECOURSE

1. ***No Pretermination***
   Assignor shall not pay nor repurchase subject security/ies before the maturity date thereof.

2. ***Liquidated Damages***
   In case of default, Assignor shall be liable, in addition to interest, for liquidated damages of _____(Amount or %)_____ plus attorney's fees of _____(Amount or %)_____ , and costs of collection in case of suit.

3. ***Delivery/Custody of Securities***
   ( ) Physically delivered to Assignee
   ( ) Evidenced by Custodian Receipt No. _____dated_____,
   issued by_____

4. ***Separate Stipulations***
   ( ) This Agreement is subject to the terms and conditions of_____ ,
   dated _____ executed by_____(name of Party/ies)_____ and
   made an integral part hereof.

Serial No:_____

_____
(Name of Quasi-Bank)

CERTIFICATE OF PARTICIPATION WITH RECOURSE

Issue Date:_____ , 20___

FOR AND IN CONSIDERATION OF PESOS _____(₱_____) , this certificate of participation is hereby issued to evidence the __(Fraction or %)__ share of ____(name of Participant)____ in the loan/s of _____ granted by/ assigned to the herein Issuer, specifically described as follows:

(Description of Debt Securities)

Principal Debtor	Serial Number/s	Maturity Date/s	Face Value	Interest/Yield
			₱	₱
TOTAL			₱	₱

The issuer shall pay, jointly and severally with the Principal Debtor, __(Fraction or %)__ share of the face value of, and the interest/yield on, said debt security(ies), subject to the terms and conditions on the reverse side hereof.

C O N F O R M E :

_____
(Duly Authorized Officer)

_____
(Signature of Participant)

NOT INSURED WITH THE PHILIPPINE DEPOSIT INSURANCE CORPORATION (PDIC)

APP. Q-6
08.12.31

TERMS AND CONDITIONS OF CERTIFICATE OF PARTICIPATION WITH RECOURSE

1. ***No Pretermination***
   Issuer shall not pay nor repurchase the participation before the maturity date of subject security(ies).

2. ***Liquidated Damages***
   In case of default, the Issuer of this instrument shall be liable, in addition to interest, for liquidated damages of __(Amount or %)__ , plus attorney's fees of __(Amount or %)__ , and costs of collection in case of suit.

3. ***Delivery/Custody of Securities***
   ( ) Physically delivered to Participant
   ( ) Evidenced by Custodian Receipt No. _____dated _____, issued by

4. ***Separate Stipulations***
   ( ) This Agreement is subject to the terms and conditions of__(describe document)__ , dated _____ executed by _____(name of Party/ies)_____ and made an integral part hereof.

Serial No: _____

_____
(Name of Quasi-Bank)

CERTIFICATE OF PARTICIPATION WITH RECOURSE

Issue Date: _____ , 20 _____

FOR AND IN CONSIDERATION OF PESOS _____, (₱ _____) this certificate of participation is hereby issued to evidence the ___(Fraction or %)___ share of ____(Participant)_____ in the loan/s of_____ granted by/assigned to the herein Issuer, specifically described as follows:

(Description of Debt Securities)

Principal Debtor	Serial Number/s	Maturity Date/s	Face Value	Interest/Yield
			₱	₱
TOTAL			₱	₱

In case of default of the Principal Debtor, the Issuer shall pay the ___(Fraction or %)___ share of the face value of, and the interest/yield on, said debt security(ies), subject to the terms and conditions on the reverse side hereof.

C O N F O R M E :

_____
(Duly Authorized Officer)

_____
(Signature of Participant)

NOT INSURED WITH THE PHILIPPINE DEPOSIT INSURANCE CORPORATION (PDIC)

APP. Q-6
08.12.31

TERMS AND CONDITIONS OF CERTIFICATE OF PARTICIPATION WITH RECOURSE

1. ***No Pretermination***
   Issuer shall not pay nor repurchase the participation before the maturity date of subject security(ies).

2. ***Liquidated Damages***
   In case of default, the Issuer of this instrument shall be liable, in addition to interest, for liquidated damages of (Amount or %) , plus attorney's fees of (Amount or %) , and costs of collection in case of suit.

3. ***Delivery/Custody of Securities***
   ( ) Physically delivered to Participant
   ( ) Evidenced by Custodian Receipt No. _____ dated _____, issued by _____ .

4. ***Separate Stipulations***
   ( ) This Agreement is subject to the terms and conditions of (describe document) dated _____ executed by (name of Party/ies) and made an integral part hereof.

NEW RULES ON REGISTRATION OF SHORT-TERM COMMERCIAL PAPERS

[Appendix to Subsec. 4235Q.10 (2008 - 4211Q.9)]

Pursuant to Presidential Decree No. 678, as amended by Presidential Decree No. 1798, and other existing applicable laws, the Securities and Exchange Commission (SEC) hereby promulgates the following new Rules and Regulations governing short-term commercial papers, in the interest of full disclosure and protection of investors and lenders, in accordance with the monetary and credit policies of the BSP.

Sec. 1. Scope. These Rules and Regulations shall apply to short-term commercial papers issued by corporations.

Sec. 2. Definition. For the purpose of these Rules, the following definitions shall apply:

(a) *Commercial paper* is an evidence of indebtedness of any corporation to any person or entity with a maturity of 365 days or less.

(b) *Interbank loan transactions* shall refer to borrowings between and among banks and NBFIs duly authorized to perform quasi-banking functions.

(c) *Issue* means creation of a commercial paper and its actual or constructive delivery to the payee.

Sec. 3. Registration of Commercial Papers. Any corporation desiring to issue commercial paper shall apply for registration with, and submit to, the SEC the following:

(a) Ordinary Registration;

(1) Sworn Registration Statement in the prescribed form;

(2) Board resolution signed by majority of its members (a) authorizing the issue of commercial paper, (b) indicating the aggregate amount to be applied for, (c) providing that the registration statement shall be signed by the principal executive officer, the principal operating officer, the principal financial officer, the comptroller, or principal accounting officer, or persons performing similar functions, and (d) designating at least two senior officers with a rank of vice-president or higher, or their equivalent, to sign the commercial paper instrument to be issued;

(3) The latest audited financial statements; and should the same be as of a date more than three (3) months prior to the filing of the registration statement, an unaudited financial statement as of the end of the immediately preceding month: *Provided, however*, That such unaudited financial statement shall be certified under oath by the accountant and the senior financial officer of the applicant, duly authorized for the purpose, and substituted with an audited financial statement within 120 days after the end of the applicant's fiscal year.

(4) Schedules A to L, based on sub-section (3) above, in the form attached as Annex "A";

(5) A committed credit line agreement with a bank, or any FI which may be qualified subsequently by the BSP, earmarked specifically for repayment of aggregate outstanding commercial paper issues on a pro-rata basis, with the following features:

(i) A firm, irrevocable commitment to make available funds to cover at least 20% of the aggregate commercial papers outstanding at any time: *Provided*, That if the commitment is extended by a group, there shall be a lead bank or any FI which may be qualified subsequently by the BSP acting for the group;

(ii) The commitment shall be effective for as long as the issues are outstanding and

may be renewed by the bank or any FI which may be qualified subsequently by the BSP;

(iii) The request for drawdown shall be addressed to the bank or any FI which may be qualified subsequently by the BSP, which request shall be duly signed by a member of the board of directors and a senior financial officer of the commercial paper issuer, duly authorized for the purpose by an appropriate board resolution, which shall also provide for the designation of the alternate signatories (likewise a member of the board of directors and a senior financial officer);

(iv) A provision that availments shall be allowed only for repayment of commercial papers which are due and payable in accordance with the terms of the commercial paper;

(v) Notwithstanding the foregoing requirements for a committed credit line with a bank, or any FI which may be qualified subsequently by the BSP, any corporation desiring to issue commercial papers may be exempted from compliance therewith by the SEC, should it meet all of the following financial ratios based on consolidated audited financial statements for the immediate past three (3) years:

1) Average current ratio shall be at least 1.2:1 computed as follows:

$$\text{Current ratio} = \frac{\text{Current Assets}}{\text{Current Liabilities}}$$

OR

Average acid-test ratios shall be at least 0.5:1 computed as follows:

$$\text{Acid-test ratio} = \frac{\text{Cash, receivables, and marketable securities}}{\text{Current Liabilities}}$$

2) Average solvency position shall be one whereby total assets must not be less than total liabilities;

3) Average net profit margin shall be at least 3% computed as follows:

$$\text{Net profit margin} = \frac{\text{Net income after income tax, corporate development taxes, and other non-cash charges}}{\text{Net sales or revenues}}$$

OR

Average annual return on equity shall be at least 8% computed as follows:

$$\text{Return on equity} = \frac{\text{Net income after income tax, corporate development taxes, and other non-cash}}{\text{Total stockholders' equity}}$$

4) Average interest service coverage ratio shall be at least 1.2:1 computed as follows:

$$\text{Interest service coverage ratio} = \frac{\text{Net income-before-interest expense, income tax, corporate development taxes, and other non-cash charges}}{\text{Interest expense}}$$

5) Debt-to-equity ratio shall not exceed 2.5:1.

The SEC may, in its discretion, consult with industry organization(s) such as Investment Houses (IHs) Association of the Philippines (IHAP) and Bankers Association of the Philippines (BAP) and/or the Credit Information Bureau, Inc.

6) A selling agreement for the commercial paper issues with an expanded commercial bank or an investment house, or any FI which may be qualified subsequently by the BSP, with minimum conditions that the selling agent, among others, shall be responsible for ensuring that the issuer observes the provisions of these rules pertaining to the use of proceeds of the committed credit line and, with the issuer, shall be jointly responsible for complying with all reportorial requirements of the SEC and the BSP in

connection with the commercial paper issue, it being understood that the primary responsibility for the submission of the report to said regulatory agencies is upon the selling agent: *Provided, however*, That if the commercial paper issuer is unable to provide the information necessary to meet such reportorial requirements, the selling agent shall, not later than two (2) working days prior to the date when the report is due, notify the SEC of such inability on the part of the issuer: *Provided, finally*, That if the selling agreement is with a group, composed of expanded commercial banks and/or investment houses or any FIs which may be qualified subsequently by the BSP, there shall be a syndicate manager acting and responsible for the group.

(7) Income statements for the immediate past three (3) fiscal years audited by an independent certified public accountant: *Provided*, That, if the applicant has been in operation for less than three years, it shall submit income statements for such number of years that it has been in operation.

(8) A printed copy of a preliminary prospectus approved by the applicant's Board of Directors which, among others, shall contain the following:

(i) A statement printed in red on the left-hand margin of the front page of the following tenor:

"A registration statement relating to these short-term commercial papers has been filed with, but has not yet been approved by, the SEC. Information contained herein is subject to completion or amendment. These short-term commercial papers may not be sold nor may offer to buy be accepted prior to the time the registration statement is approved. This preliminary prospectus shall not constitute an offer to buy nor shall there be any sale of these commercial papers in the Philippines as such offer, solicitation, or sale is prohibited prior to registration under the Securities Act, as amended by P.D. No. 678 and P.D. No. 1798."

(ii) Aggregate maximum amount applied for, stated on the front page of the prospectus;

(iii) Description and nature of the applicant's business;

(iv) Intended use of proceeds;

(v) The nature of the firm, irrevocable, and committed credit line, the amount of the line which shall be at least 20% of the aggregate outstanding commercial paper issues, proceeds of which shall be allocated on a pro-rata basis to the aggregate outstanding commercial paper issue (regardless of the order of their maturities), and the manner of availments, as stipulated in the credit line agreement between the bank and the issuer;

(vi) The provision in the selling agreement naming the selling agent and the responsibilities of the selling agent in connection with, among others, the use by the issuer of the proceeds of the bank committed credit line and the reportorial requirements under these rules;

(vii) Other obligations of the commercial issuer classified by maturities (maturing within six (6) months; from six (6) months to one (1) year; over one (1) year; and past-due amounts);

(viii) Encumbered assets;

(ix) Directors, officers, and stockholders owning 2% or more of the total subscribed stock of the corporation, indicating any advance to said directors, officers, and stockholders;

(x) List of entities where it owns more than 33-1/3% of the total equity, as well as borrowings and advances to said entities;

(xi) Financial statements for the immediate past three (3) fiscal years audited by an independent certified public accountant: *Provided*, That if the applicant has been in operation for less than three (3) years, it shall submit financial statements for such number of years that it has been in operation.

(b) *Special Registration*

In the case of special registration provided for under Section 10 hereof, the following shall, in addition to the immediately preceding requirements, be prepared and submitted by the selling agent on behalf of the applicant:

(1) Projected annual cash flow statement as of the date of filing, presented on a quarterly basis, supported by schedules on actual maturity patterns of existing receivables and liabilities (under six (6) months, six (6) months to one (1) year, over one (1) year, and past-due amounts) and inventory turnover as of the end of the month prior to the filing of the registration statement; and

(2) Complementary financial ratios for each of the immediate past three (3) fiscal years:

(i) Ratio of (a) the total of cash on hand, marketable securities, current receivables to (b) the total of current liabilities;

(ii) Debt-to-equity ratio, with debt referring to all kinds of indebtedness, including guarantees;

(iii) Ratio of (a) net income after taxes to (b) net worth;

(iv) Net profits-to-sales ratio; and

(v) Such other financial indicators as may be prescribed by the SEC. These additional data shall likewise be incorporated in the prospectus.

(c) The SEC may, whenever it deems necessary impose other requirements in addition to those enumerated in subsections (a) and/or (b) above.

Sec. 4. Commercial Papers Exempt *Per Se*. The following specific debt instruments are exempt *per se* from the provisions of these Rules:

(a) Evidence of indebtedness arising from interbank loan transactions;

(b) Evidence of indebtedness issued by the national and local governments;

(c) Evidence of indebtedness issued to the BSP under its open market and/or rediscounting operations;

(d) Evidence of indebtedness issued by the BSP, Philippine National BanK (PNB), Development Bank of the Philippines (DBP), Land Bank of the Philippines (LBP), Government Service Insurance System, and the Social Security System (GSIS);

(e) Evidence of indebtedness issued to the following primary institutional lenders: banks, including their trust accounts, trust companies, QBs, IHs, including their trust accounts, financing companies, investment companies, non-stock savings and loan associations (NSSLA), building and loan associations, venture capital corporations, special purpose corporations referred to in Central Bank Monetary Board Res. No. 1051 dated 19 June 1981, insurance companies, government FIs, pawnshops, pension and retirement funds approved by the Bureau of Internal Revenue (BIR), educational assistance funds established by the national government; and other entities that may be classified as primary institutional lenders by the BSP, in consultation with the SEC: *Provided*, That all such evidences of indebtedness shall be held on to maturity and shall neither be negotiated nor assigned to any one other than the BSP and the DBP, with respect to private development banks in connection with their rediscounting privilege, and financial intermediaries with quasi-banking functions;

(f) Evidence of indebtedness the total outstanding amount of which does not exceed ₱5,000,000 and issued to not more than ten (10) primary lenders other than those mentioned in subsection (e) above, which evidence of indebtedness shall be payable to a specific person and not to bearer and shall neither be negotiated nor assigned but held on to maturity;

(g) Evidence of indebtedness denominated in foreign currencies; and

(h) Evidence of indebtedness arising from bonafide sale of goods or property.

Sec. 5. Other Commercial Papers Exempt from Registration. Commercial papers issued by any financial intermediary authorized by the BSP to engage in quasi-banking functions shall be exempt from registration under Section 3, but shall be subject to payment of the exemption fee, as provided under Section 15, and to the reportorial requirements under Section 17, all under these Rules.

Sec. 6. Prohibition. No commercial paper, except of a class exempt under Sections 4 and 5 hereof, shall be issued unless such commercial paper shall have been registered under these Rules: *Provided*, That no registered commercial paper issuer may issue commercial paper exempt per se under Section 4 (f) hereof.

Sec. 7. Compliance with Bangko Sentral Quasi-Banking Requirements Nothing in these Rules shall be construed as an exemption from or a waiver of the applicable BSP rules/regulations or circulars governing the performance of quasi-banking functions or financial intermediaries duly authorized to engage in quasi-banking activities. Any violation of said BSP rules/regulations or circulars shall be considered a violation of these rules and regulations.

Sec. 8. Action on Application for Registration

(a) Within sixty (60) days after receipt of the complete application for registration, the SEC shall act upon the application and shall, in the appropriate case, grant the applicant a Certificate of Registration and Authority to Issue Commercial Papers.

(b) The SEC shall return any application for registration, in cases where the requirement of applicable laws and regulations governing the issuance of commercial papers have not been complied with, or for reasons which shall be so stated.

Sec. 9. Ordinary Registration. If the value of commercial papers applied for, when added to the total outstanding liabilities of the applicant, does not exceed 300% of networth based on the financial statements referred to under Section 3(a)(3), the commercial papers shall be registered upon compliance with the requirements specified in Section 3(a) hereof. The same principle shall apply in the case of renewal of the Authority to Issue Commercial Paper.

Sec. 10. Special Registration. If the value of commercial paper applied for exceeds 300% of networth, as contemplated in the preceding section, it shall be subject to compliance with the requirement under Section 3(b) hereof.

Sec. 11. Validity Period of the Authority to Issue Commercial Paper. The authority to issue commercial papers shall be valid for a period of 365 days which shall be indicated in the Authority to Issue Commercial Paper, provided that renewal thereof, upon application filed at least forty five (45) days prior to its expiry date, may be for a period shorter than 365 days.

Sec. 12. Conditions of the Authority to Issue Commercial Paper

(a) In the event that the commercial paper issuer fails to pay in full any commercial paper upon demand at stated maturity date, the Authority to Issue Commercial Paper is automatically suspended. The selling agent shall, within the next working day, notify the SEC thereof, and the SEC shall forthwith issue a formal Cease-and-Desist Order, enjoining both the issuer and the selling agent from further issuing or selling Commercial papers.

(b) Whenever necessary to implement the monetary and credit policies promulgated from time to time by the Monetary Board of the BSP, the SEC may suspend the Authority to Issue Commercial Paper, or reduce the authorized amount thereunder, or schedule the maturities of the registered commercial paper to be issued.

Sec. 13. Basic Features of Registered Commercial Papers

(a) All registered commercial paper instruments shall have a standard format, serially pre-numbered, and denominated. The instrument shall state, among others, the debt ceiling of the registrant and a notice that information about the registrant submitted in connection with the registration and other reportorial requirements from the issuer is available at the SEC and open to public inspection and that the issuer is not authorized by the BSP to perform quasi-banking functions.

(b) A specimen of the proposed commercial paper instrument shall be submitted to the SEC for approval of the text thereof.

(c) The approved instrument shall be printed by the BSP Security Printing Plant pursuant to a prior authorization from the SEC, and shall be released by the SEC to the issuer.

Sec. 14. Minimum Maturity Value The maturity value of each registered commercial paper instrument shall not be lower than ₱300,000.

Sec. 15. Fees. Every registrant shall pay the following fees:

(a) Upon application for registration, and for renewals thereof, a filing fee of not more than 1/50th of 1% based on the total commercial paper proposed to be issued.

(b) For issuers of commercial paper exempt under Section 5 hereof, an annual exemption fee of ₱10,000.

Sec. 16. Notice of Availment Whenever the credit line is drawn upon, the selling agent and/or issuer shall, within two (2) working days immediately following the date of drawdown, notify the SEC of such event, indicating the amount availed of and the total availment as of that given time.

Sec. 17. Periodic Reports

(a) Issuers of registered commercial papers and those exempt under Section 5 hereof shall submit to the SEC and the BSP the following reports in the prescribed form:

(1) Monthly reports on commercial papers outstanding as at the end of each month, to be submitted within ten (10) working days following the end of the reference month;

(2) Quarterly reports on commercial paper transactions, accompanied by an interim quarterly financial statement, to be submitted within thirty (30) calendar days following the end of the reference quarter; and

(3) For issuers whose application for registration was under Section 10 hereof, the projected quarterly cash flow statements with the corresponding quarter's actual figure, to be submitted within ten (10) working days following the end of the reference quarter;

(b) These periodic reports shall be signed under oath by the corporate officers authorized pursuant to a board resolution previously filed with the SEC;

(c) Issuers whose offices are located in the provinces may submit their reports to the nearest extension offices of the SEC.

Sec. 18. Administrative Sanctions. If the SEC finds that there is a violation of any of these Rules and Regulations and implementing circulars or that any issuer, in a registration statement and its supporting papers, as well as in the periodic reports required to be filled with the SEC and the BSP, has made any untrue statement of a material fact, or omitted to state any material fact required to be stated therein or necessary to make the statements therein not misleading, or refuses to permit any lawful examination into its corporate affairs, the SEC shall, in its discretion, impose any or all of the following sanctions:

(a) Suspension or revocation, after proper notice and hearing, of the Certificate of Registration and Authority to Issue Commercial Paper;

(b) A fine in accordance with the guidelines that the SEC shall issue from time to time: *Provided, however*, That such fine shall in no case be less than ₱200 or more than ₱50,000 for each violation, plus not more than ₱500 for each day of continuing violation. Annex "B" hereof shall initially be the guideline on the scale of fines;

(c) Other penalties within the power of the SEC under existing laws; and

(d) The filing of criminal charges against the individuals responsible for the violation.

Sec. 19. Cease-and-Desist Order. The SEC may, on its own motion or upon verified complaint by an aggrieved party, issue a Cease-and-Desist Order ex-parte if the violation(s) mentioned in Section 18 may cause great or irreparable injury to the investing public, or may amount to palpable fraud, or violation of the disclosure requirements of the Securities Act and of these Rules and Regulations.

The issuance of such Cease-and-Desist Order automatically suspends the Authority to Issue Commercial Paper.

Such Cease-and-Desist Order shall be confidential in nature until after the imposition of the sanctions mentioned in Section 18 shall have become final and executory.

Immediately upon the issuance of an ex-parte Cease-and-Desist Order, the SEC shall notify the parties involved, and schedule a hearing on whether to lift such order, or to impose the administrative sanctions provided for in Section 18 not later than fifteen (15) days after receipt of notice.

Sec. 20. Repealing Clause. These Rules and Regulations supersede the Rules on Registration of Commercial Papers dated 10 December 1975, and all the amendments to said Rules. All other rules, regulations, orders, and memoranda circular of the SEC which are inconsistent herewith are likewise hereby repealed or modified accordingly.

Sec. 21. Transitory Provision. Any authority to Issue Commercial Paper, valid and subsisting as of the date of the effectivity of these Rules and Regulations, shall remain valid and upon its expiration may, at the discretion of the SEC and subject to such conditions as it may impose, be renewed on the basis of the Rules of Registration of Commercial Papers dated 10 December 1975 for an aggregate period not exceeding fifteen (15) months from its expiry date.

Sec. 22. Effectivity. These Rules and Regulations shall take effect on 11 December 1981.

(Editors Note: Annexes "A" and "B" are not reproduced in this Appendix.)

NEW RULES ON THE REGISTRATION OF LONG-TERM COMMERCIAL PAPERS

[Appendix to Subsecs. 4235Q.10 and 4239Q.2 (2008 - 4211Q.9 and 4217Q.3)]

Pursuant to Section 4(b) of the Revised Securities Act and other existing applicable laws, the SEC hereby promulgates the following New Rules and Regulations governing long-term commercial papers, in the interest of full disclosure and protection of investors and lenders, in accordance with the monetary and credit policies of the BSP:

Section 1. Scope. These Rules shall apply to long-term commercial papers issued by corporations.

Sec. 2. Definitions. For purposes of these Rules, the following definitions shall apply:

a. *Long-term commercial papers* shall refer to evidence of indebtedness of any corporation to any person or entity with maturity period of more than 365 days.

b. *Interbank loan transactions* shall refer to borrowings between and among banks and QBs.

c. *Issue* shall refer to the creation of commercial paper and its actual or constructive delivery to the payee.

d. *Appraised value* shall refer to the value of chattel and real property, as established by a duly licensed and independent appraiser.

e. *Current market value* shall refer to the value of the securities at current prices, as quoted at the stock exchanges.

f. *Recomputed debt-to-equity ratio* shall refer to the proportion of total outstanding liabilities, including the amount of long-term commercial papers applied for, and any unissued authorized commercial papers to net worth.

g. *Specific person* shall refer to a duly named juridical or natural person as an investor for its or his own account, a trustee for one or more trustors, an agent or fund manager for a principal under a fund management agreement, and does not include numbered accounts.

h. *Net worth* shall refer to the excess of total assets over total liabilities, net of appraisal surplus.

i. *Subsidiary* shall refer to a company more than fifty percent (50%) of the outstanding voting stock of which is directly or indirectly owned, controlled, or held with power to vote by another company.

j. *Affiliate* shall refer to a concern linked, directly or indirectly, to another by means of:

1) Ownership control and power to vote of ten percent (10%), but not more than fifty percent (50%), of the outstanding voting stock.

2) Common major stockholders; i. e., owning ten percent (10%), but not more than fifty percent (50%), of the outstanding voting stock.

3) Management contract or any arrangement granting power to direct or cause the direction of management and policies.

4) Voting trustee holding ten percent (10%), but not more than fifty percent (50%), of the outstanding voting stock.

5) Permanent proxy constituting ten percent (10%), but not more than fifty percent (50%), of the outstanding voting stock.

k) *Underwriting* shall refer to the act or process of distributing and selling of any kind of original issues of long-term commercial papers of a corporation other than those of the underwriter itself, either on guaranteed or best-effort basis.

l) *Trust accounts* shall refer to those accounts with a FI authorized by the BSP to engage in trust functions, wherein there is a trustor-trustee relationship under a trust agreement.

Sec. 3. Conditions for Registration Long-term commercial papers shall be registered under any of the following conditions:

a. *Collateral*

The amount of long-term commercial papers applied for is covered by the following collaterals which are not encumbered, restricted, or earmarked for any other purpose and which shall be maintained at their respective values at all times, indicated in relation to the face value of the long-term commercial paper issue;

1) Securities listed in the stock exchanges	- Current market value of 200%
2) Registered real estate mortgage	- Appraised value of 150%
3) Registered chattel mortgage on heavy equipment, machinery, and similar assets acceptable to the Commission and registrable with the appropriate government agency	- Appraised value of 200%

b. *Financial Ratios*

A registrant who meets such standard, as may be prescribed by the SEC, based on the following complementary financial ratios for each of the immediate past three (3) fiscal years:

1) Ratio of (a) the total cash, marketable securities, current receivables to (b) the total of current liabilities;

2) Debt-to-equity ratio, with debt referring to all kinds of indebtedness, including guarantees;

3) Ratio of (a) net income after taxes to (b) net worth;

4) Net profits to sales ratio; and

5) Such other financial indicators, as may be required by the SEC.

c. *Debt to equity*

The recomputed debt-to-equity to ratio of the applicant based on the financial statements required under Sec. 4.c. hereof shall not exceed 4:1: *Provided,* That the authorized short-term commercial papers do not exceed 300% of net worth and upon compliance with the registration requirements specified in Sec. 4 hereof.

The conditions under which the commercial papers of a registrant were registered shall be strictly maintained during the validity of the Certificate of Registration.

Sec. 4. Registration Requirements Any corporation desiring to issue long-term commercial papers shall apply for registration with, and submit to, the SEC the following:

a. Sworn Registration Statement in the form prescribed by the SEC;

b. Board resolution signed by a majority of its members -

1) authorizing the issue of long-term commercial papers;

2) indicating the aggregate amount to be applied for;

3) stating purpose or usage of proceeds thereof;

4) providing that the registration statement shall be signed by any of the following: the principal executive officer, the principal operating officer, the principal financial officer, the comptroller or principal accounting officer, or persons performing similar functions; and

5) designating at least two senior officers with a rank of Vice-President, or higher of their equivalent, to sign the commercial paper instruments to be issued.

c. The latest audited financial statements and should the same be as of a date more than three (3) months prior to the filing of the registration statements, an unaudited financial statement as of the end of the immediately preceding month; *Provided, however,* That such unaudited financial statement shall be certified under oath by the accountant and the senior financial officer of the applicant duly authorized for the purpose and substituted with an audited financial statement within 105 days after the end of the applicant's fiscal year;

d. Schedules A to L based on Subsection c above, in the form attached as Annex "A";

e. Income statements for the immediate past three (3) fiscal years audited by an independent certified public accountant: *Provided*, That if the applicant has been in operation for less than three (3) years, it shall submit income statements for such number of years that it has been in operation;

f. An underwriting agreement for the long-term commercial paper issues with an expanded commercial bank or an investment house, or any other FI which may be qualified subsequently by the BSP with minimum condition, among others, that the underwriter and the issuer shall be jointly responsible for complying with all reportorial requirements of the SEC and the BSP in connection with the long-term commercial paper issue, it being understood that the primary responsibility for the submission of the report to these regulatory agencies is upon the underwriting agreement and thereafter, the responsibility shall devolve upon this issuer: *Provided, however*, That if the issuer is unable to provide the information necessary to meet such reportorial requirements, the underwriter shall, not later than two (2) working days prior to the date when the report is due, notify the SEC of such inability on the part of the issuer: *Provided, further*, That if the underwriting agreement is with a group composed of expanded commercial banks and/or investment houses or any FIs which may be qualified subsequently by the BSP, there shall be a syndicate manager acting and responsible for the group: *Provided, finally*, That the underwriter may be changed subject to prior approval by the SEC;

g. A typewritten copy of a preliminary prospectus approved by the applicant's Board of Directors which, among others, shall contain the following:

1) A statement printed in red on the left-hand margin of the front page, to wit:

"A registration statement relating to these long-term commercial papers has been filed with, but has not yet been approved by, the SEC. Information contained herein is subject to completion or amendment. These long-term commercial papers may not be sold nor may offers to buy be accepted prior to the approval of the registration statement. This preliminary prospectus shall not constitute an offer to buy nor shall there be any sale of these long-term commercial papers in the Philippines as such offer, solicitation, or sale is prohibited prior to registration under the Revised Securities Act."

2) Aggregate maximum amount applied for, stated on the front page of the prospectus;

3) Description and nature of the applicant's business;

4) Intended use of proceeds;

5) Provisions in the underwriting agreement, naming the underwriter and its responsibilities in connection with, among others, the reportorial requirements under these Rules;

6) Other obligations of the applicant classified by maturities - maturing within six (6) months; from six (6) months to one (1) year; and one (1) year and past-due amounts;

7) List of assets which are encumbered, restricted, or earmarked for any other purposes;

8) List of directors, officers, and stockholders owning two percent (2%) or more of the total outstanding voting stock of the corporation, indicating any advance to said directors, officers, and stockholders;

9) List of entities where it owns more than thirty three and one third percent (33 1/3%) of the total outstanding voting stock, as well as borrowings from, and advances to, said entities.

h. Projected annual cash flow statement presented on a quarterly basis as of the approximate date of issuance for a period co-terminus with the life time of the issue, indicating the basic assumptions thereto and supported by schedules on actual maturity patterns of outstanding receivables and liabilities (under six (6) months, six (6) months to one (1) year, over one (1) year, and past-due accounts) and inventory turnover;

i. Data on financial indicators, as may be prescribed by the SEC, for each of the immediate past three (3) fiscal years, such as on solvency, liquidity, and profitability.

The SEC may, whenever it deems necessary, impose other requirements in addition to those enumerated above.

Sec. 5. Action on Application for Registration

a. Within sixty (60) days after receipt of the complete application for registration, the SEC shall act upon the application and shall, in the appropriate case, grant the applicant a Certificate of Registration and Authority to Issue Long-Term Commercial Papers valid for one (1) year, which may be renewed annually with respect to the unissued balance of the authorized amount, upon showing that the registrant has strictly complied with the provisions of these Rules and the terms and conditions of the Certificate of Registration.

b. The SEC shall return any application for registration, in cases where the requirements of applicable laws and regulations governing the issuance of long-term commercial papers have not been complied with, or for reasons which shall be so stated.

Sec. 6. Close-end Registration Registration of long-term commercial papers under these Rules shall be a close-end process, whereby the portion of the authorized amount already issued shall be deducted from the authorized amount and may no longer be reissued even if reacquired in any manner, pursuant to the terms and conditions of issue.

Sec. 7. Long-Term Commercial Papers Exempt Per Se. The following specific long-term debt instruments are exempt per se from the provisions of these Rules:

a. Evidence of indebtedness arising from interbank loan transactions;

b. Evidence of indebtedness issued by the national and local governments;

c. Evidence of indebtedness issued by government instrumentalities, the repayment and servicing of which are fully guaranteed by the National Government;

d. Evidence of indebtedness issued to the BSP under its open market and/or rediscounting operations;

e. Evidence of indebtedness issued by the BSP, PNB, DBP, and LBP;

f. Evidence of indebtedness issued to the following primary institutional lenders: banks, including their trust accounts, trust companies,QBs, investment houses, including their trust accounts, financing companies, investment companies, NSSLAs, building and loan associations, venture capital corporations, special purpose corporations referred to in Central Bank Monetary Board Resolution No. 1051 dated 19 June 1981, insurance companies, government FIs, pawnshops, pension and retirement funds approved by the BIR, educational assistance funds established by the national government, and other entities that may be classified as primary institutional lenders by the BSP, in consultation with the SEC: *Provided,* That all such evidences of indebtedness shall be held on to maturity and shall neither be negotiated nor assigned to any one other than the BSP, and the DBP, with

respect to private development banks in connection with their rediscounting privileges, and financial intermediaries with quasi-banking functions;

g. Evidence of indebtedness, the total outstanding amount of which does not exceed ₱15.0 million and issued to not more than fifteen (15) primary lenders other than those mentioned in subsection (f) above, which evidence of indebtedness shall be payable to specific persons, and not to bearers, and shall neither be negotiated nor assigned but held on to maturity: *Provided*, That the aggregate amount of ₱15.0 million shall include outstanding short-term commercial papers: *Provided, further*, That in reckoning compliance with the number of primary lenders under this Section, holders of such papers exempt under Sec. 4(f) of the Rules on Registration of Short-Term Commercial Papers, as amended, shall be counted: *Provided, furthermore*, That such issuer shall:

1) File (1) a disclosure statement prior to the issuance of any evidence of indebtedness; and (2) a quarterly report on such borrowings in the forms prescribed by the SEC; and

2) Indicate in bold letters on the face of the instrument the words "NON-NEGOTIABLE, NON-ASSIGNABLE": and *Provided, finally*, That any issuer, in accordance with the Rules on Registration of Long-Term Commercial Papers and Bonds dated 15 October 1976 and with outstanding long-term commercial papers falling under this subsection as of the effectivity date hereof, shall likewise file the prescribed disclosure statement and the quarterly report on such borrowings;

h. Evidence of indebtedness denominated in foreign currencies; and

i. Evidence of indebtedness arising from *bona fide* sale of goods or property.

Sec. 8. Other Long-Term Commercial Papers Exempt from Registration. The following long-term commercial papers shall be exempt from registration under Secs. 3 and 4 hereof, but shall be subject to the payment of the exemption fee, as prescribed under Section 14, and to the reportorial requirements under Section 15 of these Rules:

a. Long-term commercial papers issued by a financial intermediary authorized by the BSP to engage in quasi-banking functions;

b. Long-term commercial papers fully secured by debt instruments of the National Government and the BSP and physically delivered to the trustee in the Trust Indenture.

Sec. 9. Prohibitions

a. No long-term commercial papers shall be issued, or negotiated or assigned unless the requirements of these Rules shall have been complied with: *Provided*, That no registered long-term commercial paper issuer may issue long-term commercial paper exempt per se under Section 7(g) hereof.

b. There shall be no pretermination of long-term commercial papers either by the issuer or the lender within 730 days from issue date. Pretermination shall include optional redemption, partial installments, and amortization payments; however, installment and amortization payments may be allowed, if so stipulated in the loan agreement.

Sec. 10. Compliance with Bangko Sentral Quasi-Banking Requirements Nothing in these Rules shall be construed as an exemption from, or a waiver of, the applicable BSP rules and regulations governing the performance of quasi-banking functions. Any violation of said BSP rules and regulations shall be considered a violation of these Rules.

Sec. 11. Conditions of the Authority to Issue Long-Term Commercial Papers

a. During the effectivity of the underwriting agreement, should the issuer fail to pay in full any interest due on or principal of long-term commercial paper upon demand at stated maturity date, the Authority to Issue Long-Term Commercial Papers shall be automatically suspended. The underwriter shall, within the next working day, notify the SEC thereof, and the SEC shall forthwith issue a formal Cease-and-Desist Order enjoining both the issuer and the underwriter from further issuing or underwriting long-term commercial papers.

b. Upon the expiration of the underwriting agreement, it shall be the responsibility of the issuer to notify the SEC that it failed to pay in full any interest due on, or principal of, long-term commercial paper upon demand at stated maturity date and has accordingly automatically suspended the issuance of its long-term commercial papers. Within the next working day, the SEC shall forthwith issue a formal Cease-and-Desist Order enjoining the issuer from further issuing long-term commercial papers.

c. Whenever necessary to implement the monetary and credit policies promulgated from time to time by the Monetary Board of the BSP, the SEC may suspend the authority to issue long-term commercial paper, or reduce the authorized amount thereunder, or schedule the maturities of the registered long-term commercial paper to be issued.

Sec. 12. Basic Features of Registered Commercial Papers

a. All registered commercial paper instruments shall have a standard format, serially pre-numbered, and denominated. The instrument shall state, among others, the debt ceiling of the registrant and a notice that information about the registrant submitted in connection with the registration, and other reportorial requirements from the issuer is available at the SEC and open to public inspection, and that the issuer is not authorized by the BSP to perform quasi-banking functions.

b. A specimen of the proposed commercial paper instrument shall be submitted to the SEC for approval of the text thereof.

c. The instrument approved by the SEC shall be printed by an entity authorized by the SEC and shall be released by the SEC to the issuer.

Sec. 13. Minimum Principal Amount The minimum principal amount of each registered long-term commercial paper instrument shall not be lower than the amounts indicated in the following schedule:

a. Up to two years	₱100,000
b. Over two years but less than four years	50,000
c. Four years or more	20,000

Sec. 14. Fees. Every registrant shall pay the following fees:

a. Upon application for registration, a filing fee of 1/20 of one percent 1% based on total commercial paper proposed to be issued, but not to exceed ₱75,000.

b. For issuers of commercial papers exempt under Section 8 hereof, an annual exemption fee of ₱10,000.

Sec. 15. Periodic Reports

a. Issuers of registered long-term commercial papers, through their underwriters and those exempt under Section 8 hereof, shall submit the following reports in the form prescribed by the SEC:

1) Monthly reports on long-term commercial papers outstanding as at the end of each month, to be submitted within ten (10) working days following the end of the reference month;

2) Quarterly reports on long-term commercial paper transactions, accompanied by an interim quarterly financial statement to be submitted within thirty (30) calendar days following the end of the reference quarter; and

3) Actual quarterly cash flow statement, to be submitted within ten (10) working days following the end of the reference quarter.

b. These periodic reports shall be signed under oath by the corporate officers authorized, pursuant to a board resolution previously filed with the SEC.

c. Issuers whose offices are located in the provinces may, through their underwriters, submit their reports to the nearest extension office of the SEC.

Sec. 16. Administrative Sanctions If the SEC finds that there is a violation of any of these Rules and Regulations and implementing circulars, or that any issuer, in a registration statement and its supporting papers, as well as in the periodic reports required to be filed with the SEC and the BSP, has made any untrue statement of a material fact, or omitted to state any material fact required to be stated therein or necessary to make the statements therein not misleading, or refuses to permit any lawful examination into its corporate affairs, the SEC shall, in its discretion, impose any or all of the following sanctions:

a. Suspension or revocation, after proper notice and hearing, of the Certificate of Registration and Authority to Issue Commercial Paper;

b. A fine in accordance with the guidelines that the SEC shall issue from time to time: Provided, however, That such fine shall in no case be less than ₱200 nor more than ₱50,000 for each violation, plus not more than ₱500 for each day of continuing violation. Annex "B" hereof shall initially be the guidelines on the scale of fines;

c. Other penalties within the power of the SEC under existing laws; and

d. The filing of criminal charges against the individuals responsible for the violation.

Sec. 17. Cease-and-Desist Order

a. The SEC may, on its own motion or upon verified complaint by an aggrieved party, issue a Cease-and-Desist Order ex-parte, if the violation(s) mentioned in Section 16 hereof may cause great or irreparable injury to the investing public, or will amount to palpable fraud or violation of the disclosure requirements of the Revised Securities Act and of these Rules and Regulations.

b. The issuance of such Cease-and-Desist Order automatically suspends the Authority to Issue Long-Term Commercial Paper.

c. Such Cease-and-Desist Order shall be confidential in nature, until after the imposition of the sanctions mentioned in Section 16 hereof shall have become final and executory.

d. Immediately upon the issuance of an ex-parte Cease-and-Desist Order, the SEC shall notify the parties involved, and schedule a hearing on whether to lift such order, or to impose the administrative sanctions provided for in Section 16 not later than fifteen (15) days after receipt of notice.

Sec. 18. Repealing Clause. These Rules and Regulations supersede the Rules on Registration of Long-Term Commercial Paper and Bonds dated 15 October 1976 and all the amendments to said Rules except as provided in Section 19 hereof. All other rules, regulations, orders, memoranda circular of the SEC, which are inconsistent herewith, are likewise hereby repealed or modified accordingly.

Sec. 19. Transitory Provision

a. Any authority or Certificate of Exemption to Issue Long-Term Commercial Papers, granted under the Rules on Registration of Long-Term Commercial Papers dated 15 October 1976, valid and subsisting as of the date of the effectivity of these Rules, shall remain valid with respect only to all outstanding issue until such issues are retired or redeemed.

b. The SEC may, at its discretion and subject to such conditions it may impose, authorize issuance of any unissued portion of the issuer's approved long-term debt ceiling solely for refinancing of maturing long-term commercial paper issue for a period not beyond fifteen (15) months from the effectivity date of these Rules.

Sec. 20. Effectivity. These Rules and Regulations shall take effect fifteen (15) days after publication in two newspapers of general circulation in the Philippines.

(Ed. Note: Annexes "A" and "B" are not reproduced in this Appendix.)

LIST OF RESERVE - ELIGIBLE AND NON-ELIGIBLE SECURITIES

[Appendix to Subsec. 4254Q (2008 - 4246Q.1]

A. Government securities *ELIGIBLE* as reserves

1. Direct obligations of the Government of the Republic of the Philippines eligible as reserve against peso deposit liabilities and deposit substitute liabilities:

a. 4% *PWED Bonds* all outstanding series

b. 4% *NPC Bonds* (26th - 50th Series except 39th Ser. which bear 6% - obligation assumed by the National Government)

c. 4% *Treasury Bonds* (30th S; 57th S; 59th-71st S; 78th-93rd S)

Treasury Bonds with less than 4% per annum interest considered eligible by reason of expressed BSP limited support to original purchaser:

2% T/Bond L of 1973/2003
1st Series (1st & 2nd Release)
3% T/Bond L of 1978/2008
55th Series (1st Release)
4% T/Bond L of 1979/2009
55th Series (2nd Release)
3-¼% T/Bond L of 1974/1999
6th Series (1st-2nd Release)
3-¼% T/Bond L of 1978/2003
54th Series (1st--3rd Release)

d. 4% *Treasury Notes* L of 1980/1995 115th Series

e. Bonds made specifically eligible to its holders only:

4% Treasury Capital Bonds - DBP only
2% Capital Treasury Bonds - PNB only

2. Bonds and other evidences of indebtedness bearing interest rate of four percent (4%) per annum, issued by *government-owned or controlled corporations, political subdivisions and instrumentalities* likewise eligible as reserves against peso deposit liabilities and deposit substitute liabilities:

4% NAWASA Bonds
(1st to 9th &13th Series)

3. The following government securities bearing more than four percent (4%) per annum interest, whether Bangko Sentral supported or not, if being used by banks/ QBs as reserve against deposit substitute liabilities as of 17 January 1977 shall continue to be eligible as such: *Provided,* That whenever said securities shall have matured, they shall be replaced by securities carrying the features/conditions enumerated under Circular No. 638, dated 8 November 1978, as amended:

6%	PWED Bonds	- All outstanding issues
6%	NPC Bonds	- -do
7%	NPC Bonds	- -do
8-½%	NPC Bonds	- 13th - 22nd Series
7%	MWSS Capital Bonds	- All outstanding issues
6%	NIA Bonds	- -do-
4½%	Treasury Bonds	- -do-
$4\frac{7}{10}$%	Treasury Bonds	- 7th Series
5%	Treasury Bonds	- 9th Series
6%	Treasury Bonds	- 8th Series
7%	Treasury Bonds	- All outstandingissues except 15th Series
10-¾%	Treasury Bonds	- All outstanding issues
9%	Treasury Notes	- 60th - 65th Series
10-½%	Treasury Notes	- 101st Series (1st & 2nd Release)
10-¾%	Treasury Notes	- 56th and 61st Series
11-¼%	Treasury Notes	- 59th Series
6%	NAWASA Bonds	- 11th, 12th and 1st Series
10%	EPZA Bonds	- 9th - 11th Series
10-¾%	EPZA Bonds	- 3rd - 8th Series

B. The following government securities are not eligible whatsoever for reserve purposes:

Negotiable Land Certificate (NLC)
Cultural Center of the Philippines (CCP) Bonds
Philippine Charity Sweepstakes Office (PCSO) Bonds
Public Estate Authority (PEA) Bonds
National Development Company (NDC) Bonds
National Housing Authority (NHA) Bonds
National Food Authority (NFA) Bonds
NHMFC Bahayan Certificates
Light Rail Transit Authority (LRTA) Notes
CBCIs (Auctioned/discounted) - 24th -29th Series
CBCIs (Negotiated) A to D-1Series and 5th to 7th Series (18 months)
CBCIs 10-½% Special Series 1st - 32nd Series
Central Bank Bills (Negotiated/discounted)
Treasury Bills (Negotiated/discounted)
Treasury Notes and Treasury Bonds bearing less than four percent (4%) per annum, but not given BSP support as follows:

Treasury Bonds

2% T/Bond L of 1973/2003 4th Series
2-¾% T/Bond L of 1974/1986 7-A & 7-B Series
3% T/Bond L of 1976/2001 26th, 27th, 31st - 34th, 46th & 47th Series
3% T/Bond L of 1977/2002 49th Series
3-¼% T/Bond L of 1974/1999 6th Series 3rd & 4th Release
3-¼% T/Bond L of 1977/2002 6th Series 5th Release
3-¼% T/Bond L of 1975/2000 21st Series 1st Release
3-¼% T/Bond L of 1977/2002 21st Series 2nd Release
3-¼% T/Bond L of 1977/2002 51st Series 1st & 2nd Release
3-¼% T/Bond L of 1978/2003 54th Series 1st & 34th Release
3-¼% T/Bond L of 1980/2005 58th Series
3-¾% T/Bond L of 1973/2003 2nd Series

Treasury Notes

2% T/Notes L of 1976/1991 79th Series
3% T/Notes L of 1982/1997 128th Series
3% T/Notes L of 1981/1986 120th Series & 125th Series
3-½% T/Notes L of 1982/1997 Special Series 1st-24th Release

GUIDELINES IN IDENTIFYING AND MONITORING PROBLEM LOANS AND OTHER RISK ASSETS AND SETTING UP OF ALLOWANCE FOR PROBABLE LOSSES

(Appendix to Sec. 4302Q)

I. Classification of loans. In addition to classifying loans as either current or past due, the same should be qualitatively appraised and grouped as *Unclassified* or *Classified*.

A. *Unclassified loans*. These are loans that do not have a greater-than-normal risk and do not possess the characteristics of classified loans as defined below. The borrower has the apparent ability to satisfy his obligations in full and therefore no loss in ultimate collection is anticipated. The following loans, among others, shall not be subject to classification:

1. Loans or portions thereof secured by hold-outs on deposit substitutes maintained in the lending institutions, margin deposits, or government-supported securities;

2. Loans with technical defects and deficiencies in documentation and/or collateral requirements. These deficiencies are isolated cases where the exceptions involved are not material nor is the QB's chance to be repaid or the borrower's ability to liquidate the loan in an orderly manner undermined. These exceptions should be brought to management's attention for corrective action during the examination and those not corrected shall be included in the Report of Examination under *"Miscellaneous Exceptions – Loans"*. Moreover, deficiencies which remained uncorrected in the following examination shall be classified as *"Loans Especially Mentioned"*.

The following are examples of loans to be cited under "*Miscellaneous Exceptions – Loans"*:

a. Loans with unregistered mortgage instrument which is not in compliance with the loan approval;

b. Loans with improperly executed supporting deed of assignment/pledge agreement/chattel mortgage/real estate mortgage;

c. Loans with unnotarized mortgage instruments/agreements;

d. Loans with collaterals not covered by appraisal reports or appraisal reports not updated;

e. Loan availments against expired credit line; availments in excess of credit line; availments against credit line without prior approval by appropriate authority;

f. Loans with collaterals not insured or with inadequate/expired insurance policies or the insurance policy is not endorsed in favor of the QB;

g. Loans granted beyond the limits of approving authority;

h. Loans granted without compliance with conditions stated in the approval; and

i. Loans secured by property the title to which bears an uncancelled annotation or lien or encumbrance.

B. *Classified loans*. These are loans which possess the characteristics outlined hereunder. Classified loans are subdivided into (1) *loans especially mentioned*; (2) *substandard*; (3) *doubtful*; and (4) *loss*.

1. *Loans especially mentioned*. These are loans that have potential weaknesses that deserve management's close attention. These potential weaknesses, if left uncorrected, may affect the repayment of the loan and thus increase credit risk to the QB. Their basic characteristics are as follows:

a. Loans with unlocated collateral folders and documents including, but not limited to, title papers, mortgage instruments and promissory notes;

b. Loans to firms not supported by board resolutions authorizing the borrowings;

c. Loans without credit investigation report;

d. Loans not supported by the documents required under Subsec. 4304Q.1 except:

(1) consumer loans, with original amounts not exceeding P2.0 million: *Provided*, That these loans are current, and are supported by latest ITR or by BIR Form 2316 or payslips for at least three (3) months immediately preceding the date of loan application, and financial statements submitted for taxation purposes to the BIR, as may be applicable, at the time they were granted, renewed, restructured or extended. For this purpose, consumer loans is defined to include housing loans, loans for purchase of car, household appliance(s), furniture and fixtures, loans for payment of educational and hospital bills, salary loans and loans for personal consumption, including credit card loans.

(2) Loans which are exempted from the additional documentary requirements under Subsec. 4304Q.1

e. Loans the repayment of which may be endangered by economic or market conditions that in the future may affect the borrower's ability to meet scheduled repayments as evidenced by a declining trend in operations, illiquidity, or increasing leverage trend in the borrower's financial statements;

f. Loans to borrowers whose properties securing the loan (previously well-secured by collaterals) have declined in value or with other adverse information;

g. Loans past due for more than thirty (30) days up to ninety (90) days; and

h. Loans previously cited as *Miscellaneous Exceptions* still uncorrected in the current BSP examination.

2. *Substandard*. These are loans or portions thereof which appear to involve a substantial and unreasonable degree of risk to the institution because of unfavorable record or unsatisfactory characteristics. There exists in such loans the possibility of future loss to the institution unless given closer supervision. Those classified as "*Substandard*" must have a well-defined weakness or weaknesses that jeopardize their liquidation. Such well-defined weaknesses may include adverse trends or development of financial, managerial, economic or political nature, or a significant weakness in collateral. Their basic characteristics are as follows:

a. *Secured loans*

(1) Past due and circumstances are such that there is an imminent possibility of foreclosure or acquisition of the collateral because of failure of all collection efforts;

(2) Past due loans to borrowers whose properties securing the loan have declined in value materially or have been found with defects as to ownership or other adverse information; and

(3) Current loans to borrowers whose AFSs show impaired/negative net worth except for start-up firms which should be evaluated on a case-to-case basis.

b. *Unsecured loans*

(1) Renewed/extended loans of borrowers with declining trend in operations, illiquidity, or increasing leverage trend in the borrower's financial statements without at least twenty percent (20%) repayment of the principal before renewal or extension; and

(2) Current loans to borrowers with unfavorable results of operations for two (2) consecutive years or with impaired/

negative net worth except for start-up firms which should be evaluated on a case-to-case basis.

c. Loans under litigation;

d. Loans past due for more than ninety (90) days;

e. Loans granted without requiring submission of the latest AFS/ITR and/or statements of assets and liabilities to determine paying capacity of the borrower;

f. Loans with unsigned promissory notes or signed by unauthorized officers of the borrowing firm; and

g. Loans classified as *"Loans Especially Mentioned"* in the last BSP examination which remained uncorrected in the current examination.

3. *Doubtful*. These are loans or portions thereof which have the weaknesses inherent in those classified as *"Substandard",* with the added characteristics that existing facts, conditions, and values make collection or liquidation in full highly improbable and in which substantial loss is probable. Their basic characteristics are as follows:

a. Past due clean loans classified as *"Substandard"* in the last BSP examination without at least twenty percent (20%) repayment of principal during the succeeding twelve (12) months or with current unfavorable credit information;

b. Past due loans secured by collaterals which have declined in value materially such as, inventories, receivables, equipment, and other chattels without the borrower offering additional collateral for the loans and previously classified *"Substandard"* in the last BSP examination;

c. Past due loans secured by real estate mortgage, the title to which is subject to an adverse claim rendering settlement of the loan through foreclosure doubtful; and

d. Loans wherein the possibility of loss is extremely high but because of certain important and reasonably specific pending factors that may work to the advantage and strengthening of the asset, its classification as an estimated loss is deferred until a more exact status is determined.

4. *Loss*. These are loans or portions thereof which are considered uncollectible or worthless and of such little value that their continuance as bankable assets is not warranted although the loans may have some recovery or salvage value. The amount of loss is difficult to measure and it is not practical or desirable to defer writing off these basically worthless assets even though partial recovery may be obtained in the future. Their basic characteristics are as follows:

a. Past due clean loans the interest of which is unpaid for a period of six (6) months;

b. Loans payable in installments where amortization applicable to interest is past due for a period of six (6) months, unless the loan is well secured;

c. When the borrower's whereabouts is unknown, or he is insolvent, or his earning power is permanently impaired and his co-makers or guarantors are insolvent or that their guaranty is not financially supported;

d. Where the collaterals securing the loans are considered worthless and the borrower and/or his co-makers are insolvent;

e. Loans considered as absolutely uncollectible; and

f. Loans classified as *"Doubtful"* in the last BSP examination and without any payment of interest or substantial reduction of principals during the succeeding twelve (12) months, or have current unfavorable credit information which renders collection of the loans highly improbable.

C. Credit card receivables. Credit card receivables shall be classified in accordance with age as follows:

No. of days past due	Classification
91 - 120	Substandard
121 - 180	Doubtful
181 or more	Loss

The foregoing is the minimum classification requirement. Management may therefore formulate additional specific guidelines.

II. Investments and Other Risk Assets

A. Investment in debt securities and marketable equity securities. The classification, accounting procedures, valuation and sales and transfers of investment in all debt securities and marketable equity securities is in *Appendix Q-20*.

B. Equity investment in affiliates shall be booked at cost or book value whichever is lower on the date of acquisition. If cost is greater than book value, the excess shall be charged in full to operations or booked as deferred charges and amortized as expense over a period not exceeding five (5) years. Subsequent to acquisition, if there is an impairment in the recorded value, the impairment should adequately be provided with allowance for probable losses.

C. Other property owned or acquired

1. The basic characteristics of real estate property acquired subject to *"Substandard"* classification are as follows:

a. Acquired for less than five (5) years unless worthless.

b. Converted into a Sales Contract Receivable.

c. Sold subject to a firm purchase commitment from a third party before the close of the examination.

2. The basic characteristics of real estate property acquired subject to *"Loss"* classification are as follows:

a. Foreclosure expenses and other charges included in the book value of the property, excluding the amount of non-refundable capital gains tax and documentary stamp tax paid in connection with the foreclosure/purchase which meet the criteria for inclusion in the book value of the acquired property.

b. The excess of the book value over the appraised value.

c. Property whose title is definitely lost to a third party or is being contested in court.

d. Property wherein the exercise of the right of usufruct is not practicable or possible as when it is eroded by a river or is under any like circumstances.

Real estate property acquired are not sound bank assets. Because of their nature, that is, non-liquid and non-productive, their immediate disposal through sale is highly recommended.

D. Acquired or repossessed personal property

1. All personal property owned or acquired held for three (3) years or less from date of acquisition shall be classified as *Substandard* assets.

2. The basic characteristics of acquired or repossessed personal property classified as *Loss* are as follows:

a. Property not sold for more than three (3) years from date of acquisition;

b. Property which is worthless or not saleable;

c. Property whose title is lost or is being contested in court;

d. Foreclosure expenses and other charges included in the book value of the property; and

e. The excess of the book value of the property over its appraised or realizable value.

E. Accounts Receivable

1. Accounts receivable arising from loan and investment accounts still uncollected after six (6) months from the date such loans or loan installments have matured or have become past due shall be provided with a 100% allowance for uncollected accounts receivable.

2. All other accounts receivable should be classified in accordance with age as follows, unless there is good reason for non-classification:

No. of Days Outstanding	Classification
61 - 180	Substandard
181 - 360	Doubtful
361 or more	Loss

The classification according to age of accounts receivable should be used in classifying other risk assets not covered above. However, their classification should be tempered by favorable information gathered in the review.

F. Accrued Interest Receivable

1. Accrued interest receivable on loans or loan installments still uncollected after three (3) months from the date such loans or loan installments have matured or have become non-performing shall be provided with a 100% allowance for uncollected interest on loans.

2. All other accrued interest receivable on loans or loan installments shall be classified similar to the classification of their respective loan accounts.

III. Allowance for probable losses. An allowance for probable losses on the loan accounts should be set up as follows:

A. Specific allowance

Classification	Allowance (Percent)
1. Unclassified	0
2. Loans Especially Mentioned	5
3. Substandard	
(a) Secured	10
(b) Unsecured	25
4. Doubtful	50
5. Loss	100

B. General allowance. In addition to the allowance for probable losses required under Item *"A"*, a general provision for loan losses shall also be set up as follows:

1. Five percent (5%) of the outstanding balance of unclassified restructured loans less the outstanding balance of restructured loans which are considered non-risk under existing laws, rules and regulations; and

2. One percent (1%) of the outstanding balance of unclassified loans other than restructured loans less loans which are considered non-risk under existing laws, rules and regulations.

The general loan loss provision shall be computed as follows:

For Loans Not Restructured		
Gross Loan Portfolio		₱xxx
(Excluding Restructured Loans)		
Less: Classified Loans		
(based on latest BSP examination)		
Loans especially mentioned	₱ xxx	
Substandard		
Secured	xxx	
Unsecured	xxx	
Doubtful	xxx	
Loss	xxx	xxx
Unclassified Loans		₱xxx
Less: Loans considered non-risk		
under existing regulations		xxx
Loan Portfolio, net of exclusions		₱xxx
General Loan Loss Provision		
(1% of net loan portfolio)		₱xxx
For Restructured Loans		
Restructured Loans (Gross)		₱xxx
Less: Classified Loans		
(based on latest BSP examination)		
Loans especially mentioned	₱xxx	
Substandard		
Secured	xxx	
Unsecured	xxx	
Doubtful	xxx	
Loss	xxx	xxx
Unclassified Restructured Loans		₱xxx
Less: Loans considered non-risk		
under existing regulations		xxx
Restructured Loans, net of exclusions		₱xxx
General Loan Loss Provision		
(5% of net restructured loans)		₱xxx

The excess of the booked general loan loss provisions over the amount required

as a result of the reduction of the amount required to be set up to one percent (1%) shall first be applied to unbooked specific valuation reserves, whether or not authorized to be booked on a staggered basis and only the remainder can be considered as income.

The specific and general allowances for probable losses shall be adjusted accordingly for additional allowance required by the BSP: *Provided,* That in cases of partially secured loans, only ten percent (10%) allowance shall be required for the portion thereof which are covered by the appraised value of the collateral: *Provided, further*, That said collateral is reappraised at least annually.

Management is, however, encouraged to provide additional allowance as it deems prudent and to formulate additional specific guidelines within the context of the herein-described system.

(As amended by Circular Nos. 622 dated 16 September 2008, 549 dated 09 October 2006 and 520 dated 20 March 2006)

FORMAT-DISCLOSURE STATEMENT OF LOAN/CREDIT TRANSACTION

[Appendix to Subsec. 4307Q.2 (2008 - 4309Q.2)]

_____
(Business Name of Creditor)

DISCLOSURE STATEMENT OF LOAN/CREDIT TRANSACTION (SINGLE PAYMENT OR INSTALLMENT PLAN)
(As required under R.A. 3765, Truth in Lending Act)

Name of Borrower _____

Address _____

1. Cash/Purchase Price _____ or Net Proceeds of Loan ₱ _____
   (Item Purchased)

2. LESS: Downpayment and/or Trade-in Value (Not applicable for loan transaction) _____

3. Unpaid Balance of Cash/Purchase Price or Net Proceeds of Loan _____

4. Non-Finance Charges [Advanced by Seller/Creditor]:

   a. Insurance Premium ₱ _____
   b. Taxes _____
   c. Registration Fees _____
   d. Documentary/Science Stamps _____
   e. Notarial Fees _____
   f. Others:
      _____ _____
      _____ _____
      _____ _____

Total Non-Finance Charges _____

5. Amount to be Financed (Items 3 + 4) ₱ _____

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6. Finance Charges[1]
   a. Interest _____% p.a. ₱ _____
      from _____ to _____

   [ ] Simple [ ] Monthly
   [ ] Compound [ ] Quarterly
   [ ] Semi-Annual
   [ ] Annual

   b. Discounts _____
   c. Service/Handling Charges _____
   d. Collection Charges _____
   e. Credit Investigation Fees _____
   f. Appraisal Fees _____
   g. Attorney's/Legal Fees _____
   h. Other charges incidental to the extension of credit (specify):

      _____ _____
      _____ _____
      _____ _____

   Total Finance Charges ₱ _____

7. Percentage of Finance Charges to Total Amount Financed
   (Computed in accordance with Subsec. 4307Q.1) _____%
8. Effective Interest Rate
   (Method of computation attached) _____%
9. Payment
   a. Single Payment due _____ ₱ _____
      (Date)
   b. Total Installment Payments
      (Payable in_____ weeks/months @ ₱_____) ₱ _____

[1] Time price differential should be disclosed as a finance charge. If an itemization cannot be made, a lump-sum figure may be reported among *Other charges incidental to the extension of credit* in Item *6h*.

10. Additional charges in case certain stipulations in the contract are not met by the debtor:

Nature	Rate	Amount

CERTIFIED CORRECT:

_____
(Signature of Creditor/Authorized
Representative Over Printed Name)

_____
Position

I ACKNOWLEDGE RECEIPT OF A COPY OF THIS STATEMENT PRIOR TO THE CONSUMMATION OF THE CREDIT TRANSACTION AND THAT I UNDERSTAND AND FULLY AGREE TO THE TERMS AND CONDITIONS THEREOF.

_____
(Signature of Buyer/Borrower
Over Printed Name)

DATE _____

NOTICE TO BUYER/BORROWER: YOU ARE ENTITLED TO A COPY OF THIS PAPER WHICH YOU SHALL SIGN.

ABSTRACT OF "TRUTH IN LENDING ACT" (Republic Act No. 3765)

[Appendix to Subsec. 4307Q.4 (2008 - 4309Q.4)]

Section 1. This Act shall be known as the "Truth in Lending Act."

Sec. 2. Declaration of Policy. It is hereby declared to be the policy of the State to protect its citizens from a lack of awareness of the true cost of credit to the user by assuring a full disclosure of such cost with a view of preventing the uninformed use of credit to the detriment of the national economy.

xxxx xxxx xxxx

Sec. 3. As used in this Act, the term -

xxxx xxxx xxxx

(3) "Finance charge" includes interest, fees, service charges, discounts, and such other charges incident to the extension of credit as the Board may by regulation prescribe.

xxxx xxxx xxxx

Sec. 4. Any creditor shall furnish to each person to whom credit is extended, prior to the consummation of the transaction, a clear statement in writing setting forth, to the extent applicable and in accordance with rules and regulations prescribed by the Board, the following information:

(1) the cash price or delivered price of the property or service to be acquired;

(2) the amounts, if any, to be credited as down payment and/or trade-in;

(3) the difference between the amounts set forth under clauses (1) and (2);

(4) the charges, individually itemized, which are paid or to be paid by such person in connection with the transaction but which are not incident to the extension of credit;

(5) the total amount to be financed;

(6) the finance charge expressed in terms of pesos and centavos; and

(7) the percentage that the finance charge bears to the total amount to be financed expressed as a simple annual rate on the outstanding unpaid balance of the obligation.

xxxx xxxx xxxx

Sec. 6. (a) Any creditor who in connection with any credit transaction fails to disclose to any person any information in violation of this Act or any regulation issued thereunder shall be liable to such person in the amount of ₱100 or in an amount equal to twice the finance charge required by such creditor in connection with such transaction, whichever is the greater, except that such liability shall not exceed ₱2,000 on any credit transaction.

xxxx xxxx xxxx

(c) Any person who willfully violates any provision of this Act or any regulation issued thereunder shall be fined by not less than ₱1,000 nor more than ₱5,000 or imprisonment for not less than 6 months nor more than one year or both.

xxxx xxxx xxxx

(d) Any final judgment hereafter rendered in any criminal proceeding under this Act to the effect that a defendant has willfully violated this Act shall be prima facie evidence against such defendant in an action or proceeding brought by any other party against such defendant under this Act as to all matters respecting which said judgment would be an estoppel as between the parties thereto.

Sec. 7. This Act shall become effective upon approval.

Approved, 22 June 1963.

AGREEMENT FOR THE ENHANCED INTERBANK CALL LOAN FUNDS TRANSFER SYSTEM

[Appendix to Subsecs. 4343Q.1 and 4601Q.3 (2008 - 4376Q.1 and 4601Q.1)]

(As superseded by the agreement for PhilPaSS between the BSP and BAP/CTB/ RBAP/IHAP and MMAP)

SETTLEMENT PROCEDURES FOR INTERBANK LOAN TRANSACTIONS AND PURCHASE AND SALE OF GOVERNMENT SECURITIES UNDER REPURCHASE AGREEMENTS WITH THE BANGKO SENTRAL

[Appendix to Subsecs. 4343Q.3 and 4601Q.3 (2008 - 4376Q.4 and 4601Q.1)]

(As superseded by the agreement for PhilPaSS between the BSP and BAP/CTB/ RBAP/IHAP and MMAP)

ENHANCED INTRADAY LIQUIDITY FACILITY

[Appendix to Subsecs. 4343Q.1 and 4601Q.3 (2008 - 4376Q.1 and 4601Q.1)]

Given the increasing volume of PhilPaSS transactions as well as concerns of having temporary gridlocks in the PhilPaSS, the current features of the Intraday Liquidity Facility (ILF) had been enhanced, specifically on the following areas:

a. Flexibility in changing the securities that will be used for the ILF;

b. Availment of the facility on an "as the need arises" basis; and

c. Removal of commitment fees

The revised features of the ILF are described below.

A. Access to ILF

Government securities (GS) held by an Eligible Participant QB in its Regular Principal Securities Account that will be used for ILF purposes shall be delivered to a sub-account under the BSP-ILF Securities Account with the Bureau of the Treasury's (BTr) Registry of Scripless Securities (RoSS). The delivered GS to be used for ILF purposes shall be recorded by RoSS in a sub-account (the "Client Securities Account (CSA)"-ILF) under the BSP-ILF Securities Account in the name of the Eligible Participant QB.

QBs without RoSS securities accounts who intend/desire to avail of the ILF shall be required to open/maintain a Securities Account with the RoSS. The documentation requirements for RoSS membership shall be prescribed by the BTr.

QBs desiring to avail of the ILF shall be further required to open a sub-account under the BSP-ILF Securities Account with the BTr's RoSS by accomplishing an application letter addressed to the Treasurer of the Philippines, Attn: The Director, Liability Management Service and the Chief, Scripless Securities Registration Division. The application letter shall be in the form of Annex 1 hereto.

B. Timeline

From 9:00 am to 9:30 am of each banking day, an Eligible Participant QB shall electronically instruct the BTr to move/ transfer from its Principal Securities Account with the BTr's ROSS to the CSA-ILF under the name of the Eligible Participant QB, the pool of peso-denominated GS to be set aside for the ILF purpose. The Eligible Participant QB hereby confirms to the BTr that pursuant to an ILF availment, it has authorized the transfer without consideration unto the CSA-ILF the pool of GS to be used for ILF purposes.

From 9:30 am to 10:00 am, the BTr RoSS shall electronically submit a consolidated report to BSP showing the details of the GS that were transferred to the BSP-ILF Securities Account.

From 10:00 am to 4:00 pm, Eligible Participant QBs with insufficient balances in its Demand Deposit Account No.2 (PhilPaSS Account) may avail of the ILF.

Eligible Participant QBs may avail of the ILF as necessary to fund pending payment instructions. Thus, when the ILF system detects queued transactions in the PhilPaSS-Central Accounting System, the Eligible Participant QB with insufficient balance in its PhilPaSS Account will automatically sell to the BSP-Treasury the GS in the CSA-ILF pool corresponding to the amount which may be needed to cover any pending payment instruction, and the proceeds of the sale of securities shall be immediately credited to the bank's PhilPaSS Account. There may be more than one availment during the day. Until a sale to the BSP or an Overnight Repo (O/N-RP) transaction with the BSP is

executed, the beneficial ownership of the GS that have been transferred to the CSA-ILF still belongs to the QBs.

At 5:00 pm, the BSP shall sell back to the Eligible Participant QB the GS at the same price as the original BSP purchase. Partial repayment of a particular availment will not be allowed.

In case the PhilPaSS Account balance of the participating QB is not sufficient to cover the afternoon repayment transaction, the BSP and the participating QB may agree on the following:

a. BSP shall extend to the Eligible participant QB an O/N-RP at 600 basis points over the BSP's regular overnight lending rate for the day. The O/N-RP shall be paid not later than 11:00 am on maturity date. Unpaid O/N-RP shall be automatically converted into an absolute sale to the BSP of the subject GS earlier delivered/ transferred to the CSA-ILF, pursuant to an ILF availment by the Eligible Participant QB, in which case, BSP shall issue an instruction to BTr to deliver/transfer the subject GS from the BSP-ILF Securities Account to the BSP regular Principal Securities Account. The sale shall be evidenced by the issue of Confirmation of Sale by the Eligible Participant QB (Annex 2) and the Confirmation of Purchase by the BSP Treasury Department (Annex 3), or,

b. Only in extreme cases, the BSP shall sell back to the participating QBs GS up to the extent of the PhilPaSS Account balance. The BSP shall issue an instruction to the BTr to transfer the remaining GS amounting to the unpaid ILF availment from the BSP-ILF Securities Account to the BSP's Regular Principal Securities Account.

At the end of the day and after BSP's sell-back of the GS to ILF participants, normally by 5:45 pm, the BSP Treasury Department shall electronically instruct RoSS, using the ILF RoSS system developed for herein purpose, to return/deliver from the CSA-ILF of the participating QBs to their respective Regular Principal Securities Accounts with the RoSS all unused/ unencumbered GS. GS used for O/N-RP shall remain in the CSA-ILF until repayment of subject O/N-RP or conversion to outright sale the following day.

Upon receipt of BSP's electronic instruction for the return of GS back to the participating QBs' regular Principal Securities Accounts, the BTr shall update their database after which participating QBs may request/download statements of securities accounts for their verification.

C. Eligible Securities

Peso-denominated scripless securities of the National Government that are free and unencumbered and with remaining maturity of eleven (11) days to ten (10) years shall be eligible for the ILF. GS that will be used for ILF purposes would be reclassified with due consideration to the original booking of the security, as follows:

Original Booking of GS	To be reclassified to
a. Held for Trading	Held for Trading – ILF
b. Designated Fair Value Through Profit or Loss	Designated Fair Value Through Profit or Loss - ILF
c. Available for Sale	Available for Sale - ILF
d. Held to Maturity	Held to Maturity - ILF

D. Valuation of Securities

The GS subject of an ILF transaction shall be valued based on the 11:16 am fixing rates of the previous business day, from the applicable Reuters PDEX pages or any other valuation benchmark as may be prescribed by the BSP.

E. Margins

Margins shall be applied based on prevailing policies of the BSP Treasury Department.

F. Transaction Fee

The BTr shall collect a monthly maintenance fee of One Thousand Pesos (P1,000.00) from each Eligible Participant QB for the use of the CSA-ILF Securities Account. The maintenance fees herein required to be paid by each Eligible Participant QB shall be separate from and exclusive of any other fees being assessed and collected by BTr for membership in the RoSS. For this purpose, the Eligible Participant QB shall issue to the BTr an autodebit instruction to authorize the BTr to debit its DDA with BSP for the above-mentioned monthly maintenance fee. The BTr will inform the Eligible Participant QBs of any change in fee at least fifteen (15) days prior to implementation.

G. DDA Statements/Transaction Details

Eligible Participating QBs will be able to verify the status of their accounts by initiating the SWIFT/PPS-Front-end System inquiry request.

Availability of Service

The ILF is covered by a Memorandum of Agreement (MOA) dated 25 March 2008 by and among the BSP, the BTr, the Bankers Association of the Philippines (for BAP members) and the Money Market Association of the Philippines (for non-BAP members). Participating QBs shall sign individual participation agreements. The services outlined in the MOA shall be available at the BSP and the BTr at a fixed hour on all banking days. Banking days refer to the days banking institutions are open for business, Mondays thru Fridays as authorized by the BSP.

(CL-2008-036 dated 20 June 2008)

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PARTICIPATION AGREEMENT

_____
Date

Bangko Sentral ng Pilipinas
A. Mabini corner P. Ocampo Sr. Streets,
Manila

Bureau of the Treasury
Palacio del Gobernador
Intramuros, Manila

Bankers Association of the Philippines
11th Floor, Sagittarius Building
H. V. dela Costa Street, Salcedo Village
Makati City

Money Market Association of the Philippines
Penthouse, PDCP Bank Center
Herrera corner L. P. Leviste Streets, Salcedo Village
Makati City

Gentlemen:

Please be advised that we agree to participate in the Agreement for the Establishment of Intraday Liquidity Facility to support the Philippine Payment and Settlement System (the "System") which is covered by the Memorandum of Agreement dated _____ (the "Agreement") among yourselves and its subsequent amendments of revisions as may be agreed upon by the parties thereto from time to time.

We agree to be bound by all the terms and conditions of the Agreement and adopt it as an integral part of this Participation Agreement, including the authority of the BSP to execute payment instructions and the authority of the Bureau of the Treasury (BTr) to execute our instructions on transfer to/from, credit and debit to/against our Securities Account. Further, we agree to comply with all our obligations as participating bank/financial institution as provided in the Agreement. Lastly, we agree to keep yourselves free and harmless from any claim or liability arising from, or in connection with, our transactions transmitted through the System in accordance with the provisions of the Agreement.

This participation will become effective upon your conformity hereto and your notification of the same to us, the BSP and the BTr.

Very truly yours,

_____
Participating Bank/Financial Institutions

APPROVED:

Bangko Sentral ng Pilipinas By: _____

Bureau of the Treasury By: _____

Bankers Association of the Philippines By: _____

Money Market Association of the Philippines By: _____

Annex 1

(LETTERHEAD OF THE APPLICANT)

The Treasurer of the Philippines
Palacio del Gobernador
Intramuros, Manila

Sir:

The undersigned hereby makes an application to open a Client Securities Account under the BSP-ILF RoSS Account in the Registry of Scripless Securities (RoSS) operated and maintained by the Bureau of the Treasury (BTr).

The undersigned will pay to BTr an additional monthly fee of P1,000.00 for the Client Securities Account opened payable on the first business day of each month. The BTr will inform the undersigned of any change in fee at least fifteen (15) days prior to implementation.

Please debit/credit our Regular Demand Deposit Account No._____with the BSP for the payment of said monthly fee.

_____ Manila, Philippines
(Date)

_____
(Name of Applicant)

_____
(Signature of Authorized Signatory)

_____
(Designation)

Annex 2

LETTERHEAD OF THE SELLER

Transaction No. _____
Value Date _____

CONFIRMATION OF SALE OF GOVERNMENT SECURITIES

The _____, does hereby CONFIRM that it has SOLD, TRANSFERRED AND CONVEYED unto _____, pursuant to the Memorandum of Agreement for Intraday Liquidity Facility and the Participation Agreement executed on _____ and _____, respectively, all of its rights, titles and interests over the following described Government Securities, held by the Bureau of the Treasury under the Registry of Scripless Securities System.

ISIN	TERM	ISSUE DATE	MATURITY DATE	FACE AMOUNT

_____
(Code)

_____
(Account Number)

_____
(Name of GSED)

_____
(Signature of Authorized Signatory)

_____
(Designation)

Annex 3

Transaction No. _____
Value Date _____

CONFIRMATION OF PURCHASE OF GOVERNMENT SECURITIES

The_____, does hereby CONFIRM that it has PURCHASED from _____, pursuant to the Memorandum of Agreement for Intraday Liquidity Facility and the Participation Agreement executed on _____ and _____, respectively, all of its rights, titles and interests over the following described Government Securities, held by the Bureau of the Treasury under its Registry of Scripless Securities System.

ISIN	TERM	ISSUE DATE	MATURITY DATE	FACE AMOUNT

_____ _____
(Code) (Account Number)

_____
(Name of GSED)

_____
(Signature of Authorized Signatory)

_____
(Designation)

SAMPLE INVESTMENT MANAGEMENT AGREEMENT
(Appendix to Subsec. 4411Q.1)

IMA No. (Prenumbered)

INVESTMENT MANAGEMENT AGREEMENT

KNOW ALL MEN BY THESE PRESENTS:

This AGREEMENT, made and executed this _____ day of _____ at _____ , Philippines by and between:

_____
(Hereinafter referred to as the "PRINCIPAL")

and

_____ , an institution authorized to perform trust functions, organized and existing under and by virtue of the laws of the Philippines, with principal office and place of business at _____ , _____ , Philippines.
(Hereinafter referred to as the "INVESTMENT MANAGER")

WITNESSETH: THAT -

WHEREAS, the Principal desires to avail of the services of the Investment Manager relative to the management and investment of Principal's investible funds.

WHEREAS, the Investment Manager is willing to render the services required by the Principal relative to the management and investment of Principal's investible funds, subject to the terms and conditions hereinafter stipulated;

NOW, THEREFORE, for and in consideration of the foregoing and of the mutual conditions stipulated hereunder, the parties hereto hereby agree and bind themselves to the following terms and conditions:

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INVESTMENT PORTFOLIO

1. Delivery of the Fund - Upon execution of this Agreement, the Principal shall deliver to the Investment Manager the amount of PHILIPPINE PESOS: _____(₱_____).

2. Composition - The cash which the Principal has delivered to the Investment Manager as well as such securities in which said sums are invested, the proceeds, interest, dividends and income or profits realized from the management, investment and reinvestment thereof, shall constitute the managed funds and shall hereafter be designated and referred to as the *Portfolio*. For purposes of this Agreement, the term *securities* shall be deemed to include commercial papers, shares of stock and other financial instruments.

3. Delivery of Additional Funds - At any time hereafter and from time to time at the discretion of the Principal, the latter may deliver additional funds to the Investment Manager which shall form part of the Portfolio and shall be subject to the same terms and conditions of this Agreement. No formalities other than a letter from the Principal and physical delivery to the Investment Manager of cash will be required for any addition to the Portfolio.

4. Nature of Agreement - THIS AGREEMENT IS AN AGENCY AND NOT A TRUST AGREEMENT. AS SUCH, THE CLIENT SHALL AT ALL TIMES RETAIN LEGAL TITLE TO FUNDS AND PROPERTIES SUBJECT OF THIS ARRANGEMENT.

THIS AGREEMENT IS FOR FINANCIAL RETURN AND FOR THE APPRECIATION OF ASSETS OF THE ACCOUNT. THIS AGREEMENT DOES NOT GUARANTEE A YIELD, RETURN OR INCOME BY THE INVESTMENT MANAGER. AS SUCH, PAST PERFORMANCE OF THE ACCOUNT IS NOT A GUARANTY OF FUTURE PERFORMANCE AND THE INCOME OF INVESTMENTS CAN FALL AS WELL AS RISE DEPENDING ON PREVAILING MARKET CONDITIONS.

IT IS UNDERSTOOD THAT THIS INVESTMENT MANAGEMENT AGREEMENT IS NOT COVERED BY THE PHILIPPINE DEPOSIT INSURANCE CORPORATION (PDIC) AND THAT LOSSES, IF ANY, SHALL BE FOR THE ACCOUNT OF THE PRINCIPAL.

POWERS

5. Powers of the Investment Manager - The Investment Manager is hereby conferred the following powers:

a. To invest or reinvest the Portfolio in (1) Evidences of indebtedness of the Republic of the Philippines and of the Bangko Sentral ng Pilipinas, and any other evidences of indebtedness or obligations the servicing and repayment of which are fully guaranteed by the Republic of the Philippines or loans against such government securities; (2) Loans fully guaranteed by the government as to the payment of principal and interest; (3) Loans fully secured by hold-out on, assignment or pledge of, deposits or of deposit substitutes, or mortgage and chattel mortgage bonds;

(4) Loans fully secured by real estate and chattels in accordance with Sec. 78 of R.A. No. 337, as amended, and subject to the requirements of Secs. 75, 76 and 77 of R.A. No. 337, as amended; and (5) Such other investments or loans as may be directed or authorized by the Principal in a separate written instrument which shall form part of this Agreement: *Provided*, That said written instrument shall contain the following minimum information: (a) The transaction to be entered into; (b) The amount involved; and (c) The name of the issuer, in case of securities and/or the name of the borrower and nature of security, in the case of loans;

b. To endorse, sign or execute any and all securities, documents or contracts necessary for or connected with the exercise of the powers hereby conferred or the performance of the acts hereby authorized;

c. To cause any property of the Portfolio to be issued, held, or registered in the name of the Principal or of the Investment Manager: *Provided*, That in case of the latter, the instrument shall indicate that the Investment Manager is acting in a representative capacity and that the Principal's name is disclosed thereat;

d. To open and maintain savings and/or checking accounts as may be considered necessary from time to time in the performance of the agency and the authority herein conferred upon the Investment Manager;

e. To collect and receive matured securities, dividends, profits, interest and all other sums accruing to or due to the Portfolio;

f. To pay such taxes as may be due in respect of or on account of the Portfolio or in respect of any profit, income or gains derived from the sale or disposition of securities or other properties constituting part of the Portfolio;

g. To pay out of the Portfolio all costs, charges and expenses incurred in connection with the investments or the administration and management of the Portfolio including the compensation of the Investment Manager for its services relative to the Portfolio; and

h. To perform such other acts or make, execute and deliver all instruments necessary or proper for the exercise of any of the powers conferred herein, or to accomplish any of the purposes hereof.

LIABILITY OF INVESTMENT MANAGER

6. Exemption from Liability - In the absence of fraud, bad faith, or gross or willful negligence on the part of the Investment Manager or any person acting in its behalf, the Investment Manager shall not be liable for any loss or damage to the Portfolio arising out of or in connection with any act done or performed or caused to be done or performed by the Investment Manager pursuant to the terms and conditions herein agreed, to carry out the powers, duties and purposes for which this Agreement is executed.

7. Advice of Counsel - The Investment Manager may seek the advice of lawyers. Any action taken or suffered in good faith by the Investment Manager as a consequence of the opinion of the said lawyers shall be conclusive and binding upon the Principal, and the Investment Manager shall be fully protected from any liability suffered or caused to be suffered by the Principal by virtue hereof.

ACCOUNTING AND REPORTING

8. The Investment Manager shall keep and maintain books of accounts and other accounting records as required by law. The Principal or the authorized representative of the Principal shall have access to and may inspect such books of accounts and all other records related to the Portfolio, including the securities held in custody by the Investment Manager for the Portfolio.

9. Reporting Requirements - The Investment Manager shall prepare and submit to the Principal the following reports within _____: (a) Balance Sheet; (b) Income Statement; (c) Schedule of Earning Assets; (d) Investment Activity Report; and (e) (such other reports as may be required by the Principal).

INVESTMENT MANAGER'S FEE

10. Investment Fee - The Investment Manager, in addition to the reimbursement of its expenses and disbursements in the administration and management of the Portfolio including counsel fees, shall be entitled to receive as compensation for its services a management fee of ___(Specify amount or rate)___.

WITHDRAWALS FROM THE PORTFOLIO

11. Withdrawal of Income/Principal - Subject to availability of funds and the non-diminution of the Portfolio below ₱1 million, the Principal may withdraw the income/ principal of the Portfolio or portion thereof upon written instruction or order given to the Investment Manager. The Investment Manager shall not be required to see as to the application of the income/principal so withdrawn from the Portfolio. Any income of the Portfolio not withdrawn shall be accumulated and added to the principal of the Portfolio for further investment and reinvestment.

12. Non-alienation of Encumbrance of the Portfolio or Income - During the effectivity of this Agreement, the Principal shall not assign or encumber the Portfolio or its income or any portion thereof in any manner whatsoever to any person without the prior written consent of the Investment Manager.

EFFECTIVITY AND TERMINATION

13. Term - This Agreement shall take effect from the date of signing hereof and shall be in full force and effect until terminated by either party by giving written notice thereof to the other at least _____(__) days prior to the termination date.

14. Powers upon Liquidation - The powers, duties and discretion conferred upon the Investment Manager by virtue of this Agreement shall continue for the purpose of liquidation and return of the Portfolio, after the notice of termination of this Agreement has been served in writing, until final delivery of the Portfolio to the Principal.

15. Accounting of Transaction - Within _____ (__) days after the termination of this Agreement, the Investment Manager shall submit to the Principal an accounting of all transactions effected by it since the last report up to the date of termination. Upon the expiration of the _____ (__) days from the date of submission, the Investment Manager shall forever be released and discharged from all liability and accountability to anyone with respect to the Portfolio or to the propriety of its acts and transactions shown in such accounting, except with respect to those objected to in writing by the Principal within the _____ (__) day period.

16. Remittance of Net Assets of the Portfolio - Upon termination of the Agreement, the Investment Manager shall turn over all assets of the Portfolio which may or may not be in cash to the Principal less the payment of the fees provided in this Agreement in carrying out its functions or in the exercise of its powers and authorities.

This Agreement or any specific amendments hereto constitute the entire agreement between the parties, and the Investment Manager shall not be bound by any representation, agreement, stipulations or promise, written or otherwise, not contained in this Agreement or incorporated herein by reference, except pertinent laws, circulars or regulations approved by the Government or its agencies. No amendment, novation, modification or supplement of this Agreement shall be valid or binding unless in writing and signed by the parties hereto.

IN WITNESS WHEREOF, the parties have hereunto set their hands on the date and at the place first above set forth.

_____	_____
(PRINCIPAL)	(INVESTMENT MANAGER)
By:	

SIGNED IN THE PRESENCE OF:

_____	_____

RISK MANAGEMENT GUIDELINES FOR DERIVATIVES

[Appendix to Sec. 4611Q (2008-4603Q)]

I. **Introduction**

This appendix, together with the Guidelines on Supervision by Risk *(Appendix Q-42)* and other BSP issuances on management of the different risks attendant to FI activities, provides a framework on which an FI can establish its risk management activities. Accordingly, this set of risk management guidelines for derivatives should be read and used in conjunction with all related BSP issuances on risk management.

An FI, in using these guidelines to evaluate the propriety and adequacy of its risk management, must consider the following principles:

a. No single risk management system for derivatives is expected to work for all FIs considering that the structure and level of derivatives activities will vary from one FI to another. Each FI should apply the principles set in these guidelines in a manner appropriate to its needs and circumstances. The BSP shall evaluate the quality of an FI's risk management system based on the principles and minimum requirements of these guidelines, scaled to the derivatives activities being undertaken.

b. The requirements prescribed in these guidelines are merely minimum standards and therefore, should not be taken as the "be-all" for all FI's risk management. The Board of Directors ("BOD") has the responsibility of ensuring that an FI's risk management system appropriately captures its risk exposures and affords proper management of these.

II. **Risks associated with derivatives**

While derivatives primarily help manage existing and anticipated risks, derivatives themselves are exposed to the risks they are designed to manage. Moreover, simple derivatives, when combined with other financial instruments, may result in a structure that exposes an FI to complicated risks. Thus, derivatives can aggravate the risks of FIs and of counterparties if derivatives are not clearly understood and properly managed.

A single derivatives product may expose an FI to multiple risks as enumerated under Section III of *Appendix Q-42*. These categories are not mutually exclusive of each other. Hence, derivatives activities must be managed with consideration of all of these risks.

III. **Risk management process for derivatives**

The management of derivatives activities should be integrated into an FI's overall risk management system using a conceptual framework common to the FI's other businesses. For example, price risk exposure arising from derivatives transactions should be assessed in a manner comparable to and aggregated with all other price risk exposures. Risk consolidation is particularly important because the various risks contained in derivatives and other market activities can be interconnected and may transcend specific markets.

At a minimum, the risk management process for derivatives should be able to:

a. **Identify** the risks arising from its derivatives activities in whatever capacity it deals with the same. An FI must likewise identify the impact of its derivatives activities on its overall risk profile. To properly identify risks, an FI must understand the derivatives products with which it is transacting and the factors that affect them.

Considering that changes in the value of derivatives are highly influenced by changes in market factors, risk identification should be a continuing process and should occur at both a transaction and portfolio level.

b. **Measure** the risks arising from its derivatives activities. An FI must have measurement models or tools to quantify the risks identified. These measurement tools should be suitable to the nature and volume of an FI's derivatives activities. As the complexity and volume of the derivatives activity increases, the measurement tools should correspondingly be more sophisticated. The primary criteria for the propriety of the measurement tools are accuracy, timeliness, efficiency and comprehensiveness with which these tools can capture the risks involved and their contribution to the decision-making process of FI management.

c. **Monitor** the risks arising from its derivatives activities. Derivatives products are very sensitive to market factors, which continually change. Thus, an FI should have a mechanism to monitor the responsiveness of derivatives to market factors to enable it to review and assess its risk positions. In order to effectively monitor the risks, reports must be timely generated in order to aid management in determining whether there is need to adjust the FI's derivatives positions.

d. **Control** the risks arising from its derivatives activities. An FI must establish limits to its derivatives exposure. These limits should be comprehensive and aligned with an FI's overall risk tolerance. An FI's policies and procedures on control should provide for contingencies when limits are breached. An FI must allot lead time and have a mechanism that enables management to act in time to control unacceptable or undesired exposures. An FI must also establish a system that separates functions susceptible to conflicts of interest.

IV. **Sound risk management practices for derivatives**

Consistent with the criteria for sound risk management practices in Section V of *Appendices Q-43 and Q-44*, the BSP shall assess the propriety and adequacy of an FI's risk management system for its derivatives activities in accordance with the following basic principles.

a. Active and appropriate board and senior management oversight

An FI's BOD must set the general policy or the policy direction relating to the management of an FI's risks, including those arising from its derivatives activities. This policy should be consistent with the FI's business strategies, capital strength, management expertise and risk profile. Accordingly, the BOD must understand the nature and purpose of the FI's derivatives activities and the role derivatives play in the FI's overall business strategy. Passive BOD approval is not acceptable. There must be verifiable evidence of the BOD approval processes and that senior management exerted effort to explain the nature and purpose of the derivatives activities to the BOD (e.g. minutes of BOD meetings documenting presentations and reports to the BOD and the approval processes).

The BOD must review and pre-approve new derivatives products as well as significant related policies and procedures. Central to the approval of new products is defining when a product or activity is new in order to ensure that variations on existing products receive the proper review and authorization. Policies should also detail authorized activities (e.g., at what stages approvals should be obtained, from whom approvals should be obtained), those that require on-time approval and those that are considered inappropriate.

The BOD must be apprised of the FI's derivatives exposures on a timely basis in order to enable the BOD to act on such exposures accordingly. Consequently, there

should be an established reporting methodology to ensure that the BOD receives, on a continuing basis, detailed information regarding the FI's risk exposures from derivatives, including the impact to the FI's overall risk profile, earnings and capital. These reports should include both normal and stress scenarios.

Pursuant to the general policy or policy direction on risk management set by the BOD, senior management must adopt adequate policies and procedures for conducting the FI's derivatives activities on both a long-range and day-to-day basis. Policies should clearly delineate responsibility for managing risk, and provide effective internal controls and a comprehensive risk-reporting process. Policies must also keep pace with the changing nature of derivatives products and markets and therefore must be reviewed on an on-going basis. Senior management should ensure that the various components of an FI's risk management process are regularly reviewed and evaluated. Internal evaluations may be supplemented by external auditors or other qualified outside parties.

The quality of oversight provided by the BOD and senior management to an FI's derivatives activities will be reflected in the overall risk management process, the adequacy of resources (financial, technical expertise, and systems technology) devoted to handle derivatives activities and its use of the monitoring reports. The BOD and senior management shall be responsible for ensuring that FI personnel comply with prescribed risk management standards and sales and marketing guidelines.

b. Adequate risk management policies and procedures

An FI must establish policies and procedures to guide its personnel in conducting derivatives activities. These risk management policies must be reflective of an FI's current strategy and practice.

An FI should not issue policies and procedures for derivatives in isolation. All aspects of the risk management process for derivatives activities should be integrated into the FI's over-all risk management system to the fullest extent possible using a conceptual framework common to the FI's other activities. Risk management policies should be comprehensive, covering all activities of the FI. The BSP will evaluate the degree to which controls covering derivatives activities have been integrated in other issuances of the FI covering aggregate risk-taking activities.

For FIs that conduct derivatives transactions with subsidiaries and affiliates, there should be policies and procedures that describe the nature, pricing, monitoring, and reporting of acceptable related-party transactions.

All risk management policies and procedures must be written, well-communicated to all personnel involved in the derivatives activities and readily available in user-friendly form, whether the same is a hard or soft copy thereof. An FI must also put up systems and procedures to ensure an audit trail evidencing the dissemination process for new and amended policies and procedures.

At a minimum, an FI is expected to have:

(1) Comprehensive, updated and relevant risk policy manual(s);

(2) Operations manual(s) or similar documents that describe the flow of transactions among and between the relevant units and personnel in an FI's treasury (front office, back office and accounting) and risk management unit;

(3) Approved product manual(s) that includes product definition, benefits and risks, pricing mechanisms, risk management processes, capital allocation guidelines, tax implications and other operating procedures and controls for the FI's derivatives activities.

c. Appropriate risk measurement methodologies, limits structure, monitoring and management information system

The process of measuring, monitoring and controlling risk should be carried out independently from individuals conducting derivatives activities. An independent system of reporting exposures to both senior level management and to the BOD is critical to the effectiveness of the process.

(1) Measurement methodologies

An FI must be able not only to accurately quantify the multiple risk exposures arising from its derivatives activities but also aggregate similar risks across the different activities of the FI to the fullest extent possible. An FI must develop a risk measurement model appropriate to its portfolio. Accordingly, an FI must evaluate the assumptions used, computational requirements, procedures for computing the risk metric, sourcing of inputs used in the measurement process, including the theoretical reasons for a particular input choice, and how these concepts apply to the FI's portfolio.

The risk measurement system should be structured to enable management to initiate prompt remedial action, facilitate stress-testing, and assess the potential impact of various changes in market factors on earnings and capital. A risk measurement system is considered sound if it is capable of comprehensively capturing risks from: (a) the FI's on and off-balance sheet exposure; (b) all relevant market factors; and (c) normal circumstances and stress events. Sound risk measurement practice includes identifying possible events or changes in market behavior that could have unfavorable effects on the FI and assessing the ability of the FI to withstand these events or changes. The stress testing should include not only quantitative exercises that compute potential gains or losses but also qualitative analyses of actions that management might take under particular scenarios.

An FI's risk measurement system should provide appropriate pricing and valuation procedures to ensure best execution for both proprietary trading and those undertaken for clients and a mark-to-market/model (MTM) methodology for derivatives instruments that follows established MTM regulations and Philippine Accounting Standards (PAS 39).

New measurement models, whether developed internally or purchased from vendors, should be subject to an initial validation before it is used. Internally developed models require more intensive evaluation where they have not been market-tested by external parties. The validation process should consist of a review of the logic, mathematical or statistical theories, assumptions, internal processes and overall reliability of an FI's measurement models, including the compatibility of the measurement model with the FI's technology and systems. The validation must be undertaken by a technical expert independent from the unit that developed the model. For example, pricing systems developed by a trader is required to be independently validated by a corresponding technical expert from the FI's risk management unit. If no such personnel from the risk management unit exists, an independent validation may be performed by internal audit provided that internal audit has the necessary expertise. An FI may also avail of the services of an independent outside expert. Thereafter, the frequency and extent to which models are validated depends on changes that affect pricing, risk presentation or the existing control environment. Changes in market conditions that affect pricing and risk conventions, which model performance, should trigger additional validation review.

Risk management policies should clearly address the scope of the validation process, the frequency of validations, documentation requirements, and

management responses. At a minimum, policies should require the evaluation of significant underlying algorithms and assumptions before the model is put in regular use, and as market conditions warrant thereafter. Such internal evaluation should be conducted by parties who, where practicable, are independent of the business sector using or developing the model. The evaluation may, if necessary, be conducted or supplemented with reviews by qualified outside parties, such as experts in highly technical models and risk management techniques.

(2) Limits structure

An FI must specify individual limits for all types of risks involved in an FI's derivatives activities. An FI should use a variety of limits to adequately capture the range of risks or to address risks that the measurement system does not capture. These limits should be integrated into the FI-wide limit structure to ensure consistency with the BOD-approved risk appetite and business strategy.

The limit structure should be realistic taking into consideration the target budget, level of earnings and capital. Limits must be documented and promptly communicated to all relevant personnel. Limits must be reviewed at least annually or more frequently, if circumstances warrant, in order to ensure that limits reflect the FI's past performance and current position.

Limits should be continually analyzed as regards its impact on target income, earnings and capital. These analyses should be submitted/reported to the BOD. Any excess over the limit must be approved only by authorized personnel and immediately reported to senior management and depending on the seriousness, also to the BOD. The seriousness of limit exceptions depends upon management's approach towards setting limits and on the actual size of individual and organizational limits relative to the FI's capacity to take risks. An FI with relatively conservative limits may encounter more exceptions to those limits than that with less restrictive limits. There must also be mechanisms for the correction of breach of these limits.

An FI's limit structure should address the following:

(a) Definition of a credit exposure;
(b) Maximum credit exposure to an individual counterparty;
(c) Credit concentrations;
(d) Maximum nominal exposure:
  (i) Per trader and per transaction; and
  (ii) Position limits
(e) Approved credit risk mitigation techniques; and
(f) Appropriate loss exposure triggers:
  (i) Loss alert;
  (ii) Stop loss;
  (iii) Value-at-risk; and
  (iv) Earnings-at-risk

(3) Monitoring

Monitoring of risk exposures, market conditions, and trading positions should be done at least daily. Derivatives instruments are highly influenced by movements in market factors. Thus, an FI must have a mechanism that can track and analyze the effect of market movements on its derivatives exposures. To ensure proper monitoring of risks, an FI is expected to have technology and systems that can (a) track movements in reference variables (underlying) and other market factors affecting the value of the derivatives instruments, such as trigger events; and (b) incorporate observed market movements into the pricing and valuation of derivatives instruments.

While monitoring is undertaken independently from the personnel conducting derivatives activities, FI traders are expected to actively monitor their positions to ensure that they do not breach their limits. FI traders should not wait until a limit is breached to alert senior management and risk control units. Instead, traders should promptly report unanticipated changes and progressively

deteriorating positions, as well as other significant issues arising from their positions, to the risk control function and responsible management.

(4) Management information system

An FI must institute an information system that generates accurate and incisive reports to ensure that management and the BOD are timely and regularly apprised of the FI's derivatives exposures. An FI is expected to have policies and procedures pertaining to the derivatives reporting specifying, among others, the types of derivatives reports to be generated, the purpose and contents thereof, responsible units that will generate the reports, frequency and deadlines of reports, recipients/users of reports, and the type of action expected from the users of the report. At a minimum, management reports should contain the following: outstanding derivatives positions, compliance with or status of positions as against limits, analysis of derivatives positions, along with other FI exposures, in relation to the impact to earnings and capital, monitoring of trigger events, and deviations from established policies and procedures and justifications thereof.

The management information system must be able to translate the measured risks from derivatives activities from a technical and quantitative format to one that can easily be read and understood by senior managers and directors, who may not have specialized and technical knowledge of derivatives products. Such a system enables management and the BOD to judge the changing nature of the FI's risk exposures. The electronic data processing capability must be commensurate to the volume and complexity of the FI's derivatives activities to facilitate the generation of needed reports.

The frequency and content of BOD and management reporting will ultimately depend upon the nature and significance of derivatives activities. Where applicable, BOD and management reports should consolidate information across functions and divisions. BOD and management reporting should be tailored to the intended audience, providing summary information to senior management and the BOD and more detailed information to FI traders.

Management reports should be generated by control departments independent of the risk-takers. When risk-takers provide information (e.g., valuations or volatilities on thinly traded derivatives contracts) for management reports, senior management should be informed of possible weaknesses in the data, and these positions should be audited frequently.

d. Comprehensive internal controls and independents audits.

A sound system of internal controls promotes effective and efficient operations, reliable financial and regulatory reporting, and compliance with relevant laws, regulations and policies of the FI. In determining whether an FI's internal controls meet these objectives, the BSP will consider the overall control environment of the FI, particularly, the process of identifying, measuring, analyzing and managing risk, the adequacy of management information systems, and degree of adherence to control activities such as approvals, confirmations and reconciliations. Control of the reconciliation process is particularly important where there are differences in the valuation methodologies or systems used by the front and back offices.

(1) Risk control

An FI should have an independent risk control unit responsible for the design and implementation of the FI's risk management system. A strong risk control function is a key element in fulfilling the oversight responsibilities of BOD members and senior managers. This unit must be independent from business trading units and should report directly to the BOD. The role and structure of risk control function should be commensurate to the nature, complexity and extent of an FI's derivatives activities.

A risk control unit should regularly evaluate risk-taking activities by assessing risk levels and the adequacy of risk management processes. It should also monitor the development and implementation of control policies and risk measurement systems. It should analyze daily reports produced by the FI's risk measurement model, including an evaluation of the relationship between measures of risk exposure and trading limits. Risk control personnel staff should periodically communicate their observations to senior management and the BOD.

An FI's control structure shall be considered sound if all the following elements are present:

(a) Formal approval process for new products

An FI should have an effective process to evaluate and review risks involved in products that are either new to the FI or new to the market and of potential interest to the FI. An FI that desires to engage in new products and transactions must first subject these products and transactions to a rigorous review and approval process. This will ensure that all FI personnel involved in the activity have sufficient knowledge of the product or transaction, and that the ensuing risk exposures can be identified, measured and analyzed. The process must be contained in a BOD-approved policy that is fully documented and must be implemented consistently and with integrity.

Before initiating a new derivatives activity, all relevant personnel should understand the product. Risks arising from the new product should be integrated into the FI's risk measurement and control systems. The new product approval process should include a sign-off by all relevant areas such as risk control, operations, accounting, legal, audit, and senior management and trading operations.

Defining a product or activity as "new" is central to ensuring that variations on existing products receive the proper review and authorization. Factors that should be considered in classifying a product/activity as "new" include: capacity changes (e.g., end-user to dealer), structure variations (e.g., non-amortizing swap versus amortizing interest rate swap), products which require a new pricing methodology, legal or regulatory considerations, or market characteristics (e.g., foreign exchange forwards in major currencies as opposed to emerging market currencies).

An FI should introduce new products in a manner that adequately limits potential losses and permits the testing of internal systems.

(b) Segregation of functions/units subject to conflict of interest

An FI must separate the business unit conducting the derivatives activities from the unit/s tasked with the checking, accounting, reporting and control functions of its derivatives activities.

An FI should have policies and procedures addressing conflicts of interest, particularly among the following functions: proprietary trading, sales or marketing desks/units, personal trading, and asset management.

An FI that conducts derivatives activities with its subsidiaries and/or affiliates must establish policies and procedures to avoid actual, or even the appearance of a conflict of interest. Off-market rates between related parties should generally be forbidden.

An FI should avoid dealing in transactions conducted at off-market rates. An FI should have internal policies defining what constitutes "market rates" and identify the range of deviation from the benchmark rates which could still be considered as "market rates". The FI's monitoring system should be able to alert management of any breaches in the rate tolerance levels and the appropriate action that should be taken. An FI must be able to justify any off-market transaction.

(c) Competent and adequate personnel who are properly supervised

The increased complexity of derivatives activities requires highly skilled staff particularly in the risk-taking, risk control, and operational functions. Management should regularly review the knowledge, skills and number of people needed to engage in the FI's derivatives activities. The staff must be appropriately balanced among the different areas involved in derivatives activities such that no area is understaffed in terms of number or skill.

Staff turnover can create serious problems, especially if knowledge is concentrated in a few individuals. The impact of staff turnover can be particularly acute in specialized trading markets where FI traders are in high demand and are often recruited in teams.

To mitigate business continuity and succession risk arising from a high staff turnover, an FI should devise a system of building technical expertise across involved personnel through continuous technical training, periodic rotation and cross-training of staff members performing key functions and developing understudies.

The BOD should ensure that the power and control delegated to these expert personnel are not abused. Therefore, the BOD must establish appropriate controls over their activities.

(d) Independent control functions or units

The risk control and audit units should possess the authority, independence, and corporate stature to enable them to identify and report their findings, unimpeded by FI traders. It is equally important to employ individuals with sufficient experience and technical expertise to be credible to the business line they monitor and senior executives to whom they report.

(2) Audit

Audit should be conducted by qualified professionals who are independent of the business line being audited. Audits should supplement, and not be substitute for risk control function.

The scope of audit coverage should be commensurate with the level of risk and volume of derivatives activity. The audit should include an appraisal of the effectiveness and independence of the FI's risk management process; the adequacy of operations, compliance, accounting and reporting systems; propriety of risk measurement models; and the effectiveness of internal controls. Auditors should test compliance with the FI's policies, including limits.

The level of auditor expertise should be consistent with the level and complexity of activities and degree of risk assumed. An FI may choose to outsource audit coverage to ensure that the professionals performing the work possess sufficient knowledge and experience.

Procedures should be in place to ensure that auditors are informed of significant changes in product lines, risk management methods, risk limits, operating systems, and internal controls so that the auditors can update their scope and procedures accordingly. Auditors should periodically review and analyze performance and risk management reports to ensure that areas showing significant changes are given appropriate attention.

The audit function must have the support of management and the BOD in order to be effective. Management should respond promptly to audit findings by investigating identified system and internal control weaknesses and implementing corrective action. Thereafter, management should periodically monitor newly implemented systems and controls to ensure they are working appropriately. The BOD, or designated committee, should receive reports tracking management's actions to address identified deficiencies.

(As amended by Circular No. 668 dated 02 October 2009)

SALES AND MARKETING GUIDELINES FOR DERIVATIVES
[Appendix to Sec. 4611Q (2008 - 4603Q)]

I. **General principle**

An FI, dealing with its clients, should always act with honesty, fairness and in pursuance of the best interests of its clients. Due to the complex nature of derivatives and the increasingly sophisticated products introduced into the market, an FI acting as dealer or broker must have appropriate controls and procedures to ensure the suitability of the transactions to its clients. An FI should ensure that (1) a client understands the nature of the transaction and the risks involved and (2) the transaction meets the client's financial objectives and risk tolerance. An FI should also disclose sufficient, accurate and comprehensible information about derivatives products, including inherent risks, in a clear and balanced presentation in order to enable its clients to make informed investment decisions.

These guidelines prescribe the minimum standards for sales and marketing procedures for FIs acting as dealers or brokers of derivatives.

II. **Client suitability guidelines**

An FI should ensure that the derivatives products it offers to a client are appropriate for that client through a client suitability process which involves obtaining client information, classifying a client according to his/its financial sophistication and conducting a suitability review.

a. *Client information*

An FI, at the inception of a possible business relationship with a client, should obtain from said client information about his/its financial situation, experience, and financial objectives relevant to his/its desired products/services. An FI should ensure that the client's risk and return objectives are clearly identified. This can be done through questionnaires and interviews. An FI may design and use its own system for obtaining client information that would be responsive to its client suitability process.

At a minimum, client information, including client classification, should be reviewed and updated annually or earlier, in cases of material changes in the client's financial situation or goals.

b. *Client classification*

Based on the information obtained from a client, an FI should be able to ascertain, at a minimum, a client's classification according to financial sophistication as embodied in Section 4611Q and its Subsections[1] and his/its risk tolerance. The client classification should serve as basis for an FI product/service offerings and level of disclosures required.

In dealing with corporate clients, an FI should determine whether the client is specifically authorized to enter into all or specific kinds of derivatives transactions and the person/s authorized to act in its behalf. An FI should also determine if a corporate client has competent/qualified personnel to handle the proposed derivatives activities. If a corporate client seeks to participate in highly sophisticated/more complex products, an FI should obtain written confirmation from the client that it has sophisticated risk management techniques and appropriate systems to manage and monitor the risks it will take.

In determining an individual client's classification, an FI should consider the following:

(1) The client's knowledge and understanding of derivatives transactions, related investments and the risks involved therein, including the derivatives markets;

[1] An FI, however, may adopt its own sub-classification for its own purposes.

(2) The length of time the client has been actively dealing with investment and/or derivative products, the frequency of dealings and the extent to which he has relied on the investment advice of an FI or any financial advisor, if any;

(3) The size and nature of investment transactions that have been undertaken by the client; and

(4) The client's financial standing, which may include an assessment of his net worth or the value of his portfolio.

An FI must make a record of the classification under which each client is categorized, including sufficient information to support the categorization.

Only banks with Type 1 authority or FIs with Type 2 authority may originate or distribute authorized derivatives products to non-sophisticated end-users for investment purposes. Non-sophisticated end-users should be provided greatest protection compared to all other client types.

c. *Suitability review*

Before presenting, proposing or recommending a particular derivatives product to a client, a dealer should determine that the derivatives product is suitable to the client's financial situation and consistent with the clients' mandates, financial objectives and constraints.

At a minimum, an FI should consider the following in choosing the derivatives products/services offerings to its clients:

(1) Investment amount or investible funds;

(2) Concentration ratio (i.e., asset allocation of the client's investible funds);

(3) Purpose for transacting in derivatives transaction (e.g., hedging vs. investment; long-term buy and hold as opposed to short-term active trading);

(4) Holding period or investment horizon;

(5) Client's regulatory and legal circumstances;

(6) Liquidity needs;

(7) Returns objectives (e.g., income, growth in principal, maintenance of purchasing power);

(8) Risk tolerance; and

(9) Client's understanding of the risks.

An FI should maintain a record of all the information as bases of its suitability assessment. It is highly recommended that an FI requires a client to sign its conformity to the suitability assessment (including the information basis of the assessment) in order to avoid disputes with the client on its suitability assessment.

For non-sophisticated clients, an FI should adopt a suitability statement explaining simply and clearly why the product offered is viewed suitable, considering the client's needs and preferences. To ensure the statement will be effective, an FI should consider the following features:

(1) Simple and plain language: when technical terms need to be incorporated, they should be explained if the client is unlikely to understand their meaning; and

(2) Concise and clear messages: lengthy explanations and extensive statements are likely to reduce the effectiveness of the statement and make the client less likely to read the statement properly.

Ideally, each suitability letter for non-sophisticated clients will be different, reflecting the approach taken by the FI representative in obtaining client information, the derivatives product presentation, the client's profile and considerations on which the investment proposal was based, all of which involve professional judgment. An FI, however, can apply a degree of standardization to aid quality control. An FI should clearly link its proposed or recommended derivatives product to the client's own needs, priorities and attitude toward risk. An FI may mention alternative products suitable for the client. The suitability letter should be signed by the

client and the officer authorized by the FI to advise/sell/propose the recommended product.

An FI does not need to comply with the requirement of suitability review in cases where the client is classified as a market counterparty, considering its recognized sophistication. However, an FI should be able to provide sufficient support for its classification.

III. **Disclosures**

An FI should always be mindful of its statements regarding its products/services, whether the statements pertain to promotion, marketing or sale thereof or in the course of making the required disclosures. An FI must institute measures to ensure that its clients understand the nature and risks in a derivatives transaction. These procedures may vary with the sophistication of its client. An FI can tailor-fit information, marketing and sales presentations/materials in accordance with the client classification under Sec. 4611Q and its Subsections. An FI should take further steps to adequately disclose the attendant risks of specific types of transactions when dealing with an unsophisticated client, either generally or with respect to a particular derivatives transaction (e.g., non-sophisticated client or sophisticated client with respect to complex product types). An FI should adopt standards for its publications/materials/disclosure statements and review the aforementioned documents regularly to ensure that they meet the standards.

An FI, when providing information to its clients, including potential clients, must not knowingly misrepresent or give a false impression in any of its advertisements, electronic communications, written materials (whether publicly disseminated or not) or oral representations regarding the financial derivatives offered. A misrepresentation is any statement that deviates from the truth or omits a material fact or even tends to mislead the recipients.

a. *Financial promotion (marketing and sales)*

An FI embarking on a financial promotion, whether through a direct offer or information/sales publications, should ensure it gives sufficient information to enable a client to make an informed assessment of the derivatives transaction, including its underlying. An FI must prominently indicate its name in all its promotional materials and must specify its role or capacity in the transaction (e.g., as issuer, dealer/distributor, broker).

A financial promotion is considered clear, fair and not misleading if all the following requisites are present:

(1) Any statement of fact, promise or prediction is clear, fair and not misleading. A statement should disclose relevant assumptions;

(2) A client, by himself, can discern from the presentation whether the statement is a fact, promise or prediction.

(3) The accuracy of all material statements of fact can be substantiated.

(4) Any comparison or contrast of a product offered should be with another investment intended to meet the same needs or to serve the same purpose. The facts on which any comparison or contrast is made are verified, or alternatively, that relevant assumptions are disclosed. The comparison or contrast should be presented in a fair and balanced way and includes all factors which are relevant to the comparison or contrast.

(5) The design, content or format of any presentation does not disguise, obscure or diminish the significance of any statement, warning or other matter which the presentation should contain;

(6) Disclosures on risks and warnings should not be less prominent than any other information on performance;

(7) No reference to an approval by a regulatory body or its officials shall be made,

unless a written approval was actually obtained;

(8) A recommendation to consult/refer to a financial advisor, if the client has doubts on suitability of derivatives product; and

(9) It does not omit any information, the omission of which causes a material fact to be misleading, unclear or unfair;

An FI should consider the client's knowledge of the transaction to which a given information relates. An FI should not assume that clients/recipients necessarily have an understanding of the derivatives product being promoted. An FI should assess its usage of terms, especially those which are technical. If promotional or marketing materials are specially designed for a targeted client base reasonably believed to have particular knowledge of the investment, this should be made clear in the materials.

b. *Product disclosures*

An FI must endeavor to explain the derivatives products it offers to its client to enable the latter make an informed investment decision. Product disclosures should present an adequate description of at least (a) the nature of the derivatives product, including the underlying, (b) the amount of investment required and (c) the risks involved. The adequacy of description depends on the target client classification and type of product offered. In general, disclosure should always be presented in a balanced manner where the potential benefits of an investment are tempered by a fair indication of the risks involved.

A product disclosure, which includes an illustration of past or future performance of the derivatives product or its underlying, must comply with the following:

(1) When using past performance of a derivatives instrument, or its underlying, to illustrate possible returns, the disclosure should state that past performance is not necessarily indicative of future performance. This should be presented in the main text of presentation material. Past performance must be culled from a sufficient time frame to provide a fair and balanced indication of performance; and

(2) When using any forecast on the economy, stock market, bond market and economic trends of markets, the disclosure should state that such forecast is not necessarily indicative of the likely or future performance of the instruments; and

(3) Illustrations of returns should include worst case scenarios (i.e., not just the likely or best scenarios). Benefits shown in headline rates (pro-forma returns highlighted) should be realistic and achievable, and not based on unreasonably optimistic view of events;

Product disclosures for derivatives products with some form of guarantee or protection must highlight which benefits are guaranteed/protected and those which are not. In case of structured deposit products, an FI must ensure that any representation or claim of the Philippine Deposit Insurance Corporation ("PDIC") guarantee should have been pre-cleared with the PDIC. In instances where the guarantee or protection involves a cost to the client, the FI must disclose the fee or charge for the same. An FI should also disclose the counterparty (e.g., issuer/guarantor) risk involved to clients so that they are not misled about the capital security/principal protection. An FI, when applicable, should state if the guaranteed or protected amount is payable only at the end of the term.

Product disclosures for leveraged products/transactions[1] should emphasize that while these types of products/strategies amplify the potential gain from an investment, they also increase the potential loss thereof. A client who intends to engage in margin buying, a means of applying leverage in investing, must be cautioned on possible loss exceeding the margin or initial cash outlay.

[1] Leverage or gearing can be employed in a structured product to be able to offer high yields.

c. *Minimum required disclosures*

The minimum required disclosure should always be in writing. Except for a market counterparty, an FI should require its client to sign or initial the disclosure statement as affirmation of the client's receipt and understanding of the disclosure statement. An FI may opt to draft individual and separate suitability assessment and disclosure statement to its client or consolidate the same into a separate document or incorporate these with the main derivatives transaction agreement/contract.

Product-specific minimum disclosure should include:

(1) The nature of the derivatives product, including the underlying financial instruments and how these instruments work;

(2) Investment horizon or tenor of financial derivatives;

(3) Fees and charges, whether embedded in the structure or not;

(4) Details on the issuing entity in case the dealing FI is not the issuing institution, (i.e., the FI acts as a broker/dealer, market maker);

(5) Returns or benefits likely to be derived from the instrument, the amount and timing thereof and whether the benefits are guaranteed or not.

(6) All risk factors that may result in the client receiving returns less than the illustrated returns and factors affecting the recoverable amount by the client;

(7) Details of conflicts of interest, if any

(8) All termination clauses, when appropriate, including charges and restrictions[1].

(9) Any warning, exclusion or disclaimer in relation to the product, including, but not limited, to the following:

(a) The derivatives products carry higher risks than those associated with ordinary FI savings or time deposits.

(b) The transactions are risky and may not be appropriate if client is not willing or able to accept the risk of adverse movements in the underlying securities/ reference rates.

(c) Past performance of the underlying reference is not a guarantee of future performance.

When applicable, an FI should draw the attention of the client to the following:

(i) The effect of early redemption of a product on the return (e.g., penalties and a poor return);

(ii) The availability of maximum benefits advertised after a specified period;

(iii) The pre-requisite conditions for the advertised growth rate of income;

Complex products must carry a standard warning that they are not suitable for all clients, and are intended for experienced and sophisticated investors. Complex products should carry appropriate warnings on the high economic risks of complex derivatives transactions, such as:

(i) Loss of all or a substantial portion of the investment due to leveraging or other sophisticated practices;

(ii) Volatility of returns;

(iii) Lack of liquidity considering that there may be no secondary market for the instrument;

(iv) Restrictions on transferring interests; and

(v) Absence of information regarding valuation and pricing.

Appendix Q-16A contains sample disclosure statements which an FI may adopt in accordance with the features of the derivatives product offered.

IV. Sales and marketing personnel

Any informational or promotional presentation regarding derivatives products should be undertaken only by personnel who are knowledgeable on derivatives products involved. An FI, in assessing its personnel's

[1] For instance, for a structured deposit, the FI should ensure that the customer is fully aware of the tenor of the deposit and that the principal amount is only guaranteed if held to maturity.

knowledge in derivatives transactions, may consider the personnel's educational background, relevant training, professional experience in rendering investment advice, making presentations regarding derivatives products or assessing the propriety of investment products for a client. Personnel involved in derivatives transaction must likewise be familiar with all relevant laws, applicable rules and regulations and must ensure compliance therewith.

At a minimum, an FI should establish qualification standards for personnel involved in derivatives activities as well as comply with certification requirements prescribed by existing securities laws, rules and regulations. In addition, an FI should implement, and maintain a reasonably comprehensive system of training of personnel geared at enhancing technical knowledge of its personnel to enable them to understand, explain the nature and risks of an FI's derivatives products and ensure client suitability.

The FI's BOD and senior management shall be liable to its clients for the acts performed and representations made by sales and marketing personnel in their official capacity. Notwithstanding the foregoing, an FI's BOD and senior management are not precluded from filing the necessary action against the erring sales and marketing personnel.

In order to avoid client confusion between FI deposit products and derivatives transactions, an FI should physically separate the frontline personnel and premises involved for traditional FI products from derivatives transactions.

(As amended by Circular No. 668 dated 02 October 2009)

SAMPLE RISK DISCLOSURE STATEMENT FOR DERIVATIVES ACTIVITIES

[Appendix to Sec. 4611Q (2008 - 4603Q)]

While derivatives instruments are utilized for hedging or managing investment risk, derivatives instruments themselves involve a variety of significant risks. Considering the complexity of derivatives products, these products are generally unsuitable for non-sophisticated investors.

You should not deal in derivatives products unless you understand their nature and the extent of your exposure to the attendant risks. And even assuming that you understand derivatives transactions, you should not deal with the same unless the product is suitable for you in the light of your circumstances, experience, financial position and operational resources.

As in any financial transaction, you should ensure that you understand and comply with the regulatory requirements applicable to you and/or limitations set by your BOD or other governing body. You should also consider the legal, tax and accounting implications of entering into any derivatives transaction.

This product generally carries higher risks than those associated with ordinary FI investments and therefore not a suitable substitute for savings or time deposits. These transactions are risky and may not be appropriate if you are not willing or able to accept the risk of adverse movements in the underlying securities/reference rates.

This transaction does not guarantee a yield, return or income. Past performance of the reference rate or similar instruments is not a guarantee of future performance. The income from the transaction may or may not fluctuate depending on prevailing market conditions.

(An FI need not adopt all the following enumerated statements. It only has to incorporate those statements that may be applicable to the derivatives products or transactions).

(1) *This transaction may be used for hedging purposes. If you are entering into the transaction for hedging purposes, this product may not match your exposure perfectly. You may be under or over hedged or may be subject to other exposures as a result of the transaction.*

(2) *These are over-the-counter derivatives which may pose liquidity risks to you. These are generally not liquid because there is no exchange or secondary trading market through which you can dispose the derivative. Bid and offer prices for these instrument may not be quoted. Bid and offer quotes, if any, are established by the dealers in the instruments and consequently fair price may be difficult to establish.*

(3) *While you may terminate this transaction prior to the specified termination date, the cost of early termination may be substantial. Pre-termination may reduce the expected return or the investment amount, even in the case of principal protected structured products.*

Product specific disclosures

(1) *This transaction can be subject to the risk of loss of the entire principal/notional amount of the transaction. You may lose some or all of your investment.*

(2) *(For principal protected structured products) While the principal for structured deposits may be protected and carries PDIC guarantee, returns are variable and often contingent on the performance of complex financial instruments that an average customer may not fully understand. There is still a potential loss of the principal amount invested if the structured deposit is not held to maturity, i.e., there is an early redemption fee.*

(3) *(For leveraged products/transactions) If the derivatives transactions require you to put up a margin, you may sustain a loss of the entire margin you deposited with the FI to*

establish or maintain your position. If the market moves against you (i.e., unfavorably), you may even be called upon to pay additional margin (known as margin call) at short notice to maintain the position. If you fail to do so within the time required, your position may be liquidated at a loss and you will be responsible for the resulting deficit.

(4) *(For non-readily realizable investments) You may have difficulty selling this investment at a reasonable price and, in some circumstances, it may be difficult to sell it at any price. Do not invest in this unless you have carefully thought about whether you can afford it and whether it is right for you.*

(5) *These instruments often involve a high degree of gearing or leverage, so that a relatively small movement in the price of the underlying asset or variable can result in a much larger movement, unfavorable or favorable, in the price of the instrument. The price of the instrument can therefore be volatile.*

(6) *In buying options, the maximum loss can be limited to the premium (plus any commission or transaction charges) when the price of the underlying asset moves against you because you can simply allow the option to lapse. However, if you buy a call option on another derivatives instrument, e.g., futures contract, the exercise of the option may expose you to the risks for that particular derivatives.*

(7) *If you write an option, the risks are considerably greater. You may be liable for margin (i.e., minimum level of collateral) to maintain your position and a loss may be sustained well in excess of the premium received. By writing an option, you are accepting a legal obligation to purchase or sell the underlying asset if the option is exercised against you, however far the exercise price may have moved from the market price of the underlying asset. If you already own the underlying asset (known as covered call option), the risk is reduced. However, if you do not own the underlying asset, the risk can be unlimited. Only experienced persons should contemplate writing uncovered options, and then only after securing full details of the applicable conditions and potential risk exposure.*

Any scenario analysis is being provided for illustrative purposes only. It does not represent actual prices that may be available to you. It does not present all possible outcomes or describe all factors that may affect the value of the transaction.

No advice on investments has been given. If you have any doubt about the suitability of the product, you should contact a financial advisor or carefully consider whether the product is suitable for you.

In entering into any derivatives activity with or arranged by us, you should understand that we are not acting in the capacity of your financial adviser due to the inherent conflicts of interests in simultaneously acting as dealer and financial adviser. Notwithstanding the conflict of interest, we may act as your financial adviser only if you have so agreed in writing and only to the extent so provided.

THIS STATEMENT DOES NOT PURPORT TO DISCLOSE ALL OF THE RISKS OR RELEVANT CONSIDERATIONS IN ENTERING INTO DERIVATIVES TRANSACTIONS. YOU SHOULD REFRAIN FROM ENTERING INTO ANY SUCH ACTIVITY UNLESS YOU FULLY UNDERSTAND ALL SUCH RISKS AND HAVE INDEPENDENTLY DETERMINED THAT THE ACTIVITY IS SUITABLE FOR YOU.

[Name of FI]

I/We have read and understood the risk warning set out above.

Date

[Signature of Customer]

(Circular No. 668 dated 02 October 2009)

(RESERVED)

SECURITIES AND EXCHANGE COMMISSION BASIC RULES AND REGULATIONS TO IMPLEMENT THE PROVISIONS OF PRESIDENTIAL DECREE NO. 129, OTHERWISE KNOWN AS "THE INVESTMENT HOUSES LAW"

[Appendix to Secs. 4903Q and 4106Q (2008 - 4604Q and 4656Q)]

To effectively carry out the provisions of Presidential Decree (P.D.) No. 129, otherwise known as "The Investment Houses Law", the Commission, pursuant to the powers vested in it by said Decree, and by R.A. Nos. 1143 and 5050, hereby promulgates the following rules and regulations for the information and guidance of the public:

Section 1. Scope of Applicability. These rules and regulations shall apply to any enterprise which engages or purports to engage in the underwriting of securities.

Sec. 2. Definitions. The following terms as used in P.D. No. 129 and these rules shall be understood to mean as follows:

a) *Investment House* (IH) is any enterprise which engages or purports to engage, whether regularly or on an isolated basis, in the underwriting of securities of another person or enterprise, including securities of the Government and its instrumentalities.

b) *Underwriting of securities* is the act or process of guaranteeing the distribution and sale within the Philippines of securities issued by another person or enterprise, including securities of the Government or its instrumentalities. The distribution and sale may be on a public or private placement basis.

c) *Securities* are written evidences of ownership, interest or participation, in any enterprise, or written evidences of indebtedness of a person or enterprise. It includes, but is not limited to, the instruments enumerated in Section 2 of the Securities Act.

d) *Guarantee* is any commitment and/or undertaking made by a person, firm or entity to an issuer or holder of securities to raise funds for said issuer or holder, by the distribution of such securities for sale, resale, or subscription, either through an outright purchase or through a corresponding commitment to purchase the balance not subscribed or sold.

e) *Private placement* refers to the underwritten sale of securities to less than 20 persons or enterprises.

f) *Public distribution* refers to the underwritten sale of securities to at least 20 persons or enterprises.

g) *Voting stock* is that portion of the authorized capital stock of an IH, as are subscribed and entitled to vote.

h) *Paid-in capital* are all payments on subscriptions to the authorized capital of an IH, including premiums paid in excess of par.

i) *Officer* shall be understood to mean a senior officer of an IH or bank, which includes the president, executive vice-president, general manager, vice-president, assistant vice-president, corporate secretary, head of an operating department and branch manager and such other officers as the Commission, in consultation with the BSP, shall determine.

j) *Organizers* are persons who undertake to form an IH, among themselves and others, and who are indicated in the articles of incorporation as the incorporators and the incorporating directors.

k) *Managerial staff* are the officers of an IH. Where an IH is under a management contract the terms shall be understood to include the officers of the management firm.

l) *Unimpaired capital and surplus* means the total of the unimpaired paid-in capital, surplus, and undivided profits net of such valuation reserves as may be required by the Commission provided that the Commission may include such other items as it may deem appropriate.

m) *Quasi-banking functions* shall refer to the functions defined as such by law and appropriate implementing rules and regulations.

n) *Commission* shall mean the Securities and Exchange Commission.

Sec. 3. Organization and Registration

A. *Investment Houses* shall be organized in the form of stock corporations in accordance with the provisions of the Corporation Law, subject to the following requirements:

1) At least a majority of the voting stock of the corporation shall be owned by citizens of the Philippines. In determining the percentage of foreign-owned voting stocks in an IH, the basis of the computation shall be the citizenship of each stockholder, and, with respect to corporate owners of voting stock, the citizenship of the individual owners of voting stock in the corporation holding shares in the IH;

2) The majority of the members of the Board shall be citizens of the Philippines;

3) Foreign equity participation shall be registered or reported with the Board of Investment in accordance with the rules and regulations of that Office, prior to or simultaneous with the registration with the Commission;

4) The corporation shall have a minimum initial paid-in capital of ₱20.0 million at the time of incorporation;

5) Resident foreign directors or technicians of an IH, if any, shall register with the Bureau of Immigration and Deportation;

6) In no event shall an officer of an IH be at the same time an officer of a bank, as defined in Section 3 of R.A. No. 337, as amended;

7) No director or officer of an IH shall at the same time be a director of a bank, and no director of an IH shall at the same time be an officer of a bank, except as may be authorized as an exception by the Monetary Board of the BSP.

B. *Procedure* - The organizers shall file with the Commission, a sworn application for registration in accordance with the prescribed form, together with the following documents:

(1) All documents required for registration as a stock corporation;

(2) An information sheet of the registrant corporation; [SEC Form 129-2]

(3) A statement under oath by the organizers and the proposed managerial staff, of their educational background and work experience, as well as information on any position currently held by them in banking and other FIs, if any (SEC Form 129-3);

(4) A one-year projected statement of assets and liabilities of the proposed IH;

(5) A tentative program of operation for one year, including its investment direction and volume, its expected sources and intended uses of funds and its quasi-banking functions, if any.

C. *Hearing on Application* - The Commission shall conduct a hearing to determine whether the establishment of the proposed IH will promote public interest and economic growth. The BSP shall be officially notified. The SEC Commissioner shall not register any articles of incorporation unless his Office shall have consulted the BSP and is satisfied on the basis of the evidence submitted that:

(1) All the requirements of P.D. No. 129 and of existing laws relative to the organization of an IH have been complied with;

(2) Public interest and economic growth are promoted;

(3) The amount of capital, the proposed organization, direction and

administration, as well as the integrity, experience and expertise of the organizers and the proposed managerial staff, provide reasonable assurance that the enterprise will be conducted with financial prudence.

D. *Issuance of Certificate of Incorporation* - Upon compliance with all the requirements of law and implementing rules, and the Commission is satisfied that the formation of the IH will promote public interest and economic growth, a Certificate of Incorporation will be issued to it. A license to operate shall also be granted after it shall have adopted its by-laws, elected its directors and appointed its officers.

E. *Annual Fees* - On or before the fifteenth day of January of each year, and for as long as its license to operate remains in effect, each IH shall pay a fee of ₱200. At the time of payment, the Commission may require the licensee to appear and inform the Commission of the results of its operations.

F. *Branch Operations* - No IH shall open, maintain or operate a branch or agency without first securing from the Commission a license to operate a branch in a particular locality. All applications for a license to operate a branch shall be acted upon by the Commission within ninety (90) days after submission of such documents as may be required by the Commission in support of such application.

G. *Use of the Term "Investment House"* - No person, association, partnership or corporation other than those duly licensed as an IH in accordance with these rules and regulations, shall advertise or hold itself out as being engaged in the business of an IH.

Sec. 4. Underwriting Requirements Underwriting agreements entered into by an IH, with respect to public distribution of securities, including the fees to be charged in connection therewith, shall be subject to the approval of the Commission, it being understood that no public distribution of securities shall be made without such approval. The Commission may impose such terms and conditions as may be necessary in the public interest and for the protection of investors; and it may require the submission of such documents as may be necessary to ascertain compliance with such standards of operation as it may establish. Transactions which constitute quasi-banking functions shall be subject to BSP regulation.

As a gesture of faith in the issue, an IH may take for its own account a portion of the securities it underwrites but shall sell such securities to the public.

Sec. 5. Management of Funds. The Commission, by circular, shall provide limitations on investments of discretionary accounts under the management of an IH.

Should the IH engage in the management of funds, it must at all times adhere to the prudent man's rule. The IH shall ensure that the interest of the funds managed is promoted and that the operation of the funds is undertaken on an arms' length basis.

The Commission may require such documents and reports as may be necessary, in order to determine if prudence and safety of the principal have been paramount in the decision of the IH.

Sec. 6. Underwriting Fees. Except in highly meritorious cases, as approved by the Commission, an IH shall not collect underwriting fees in excess of five percent (5%) of the amount generated by the underwriter for the issuer.

Sec. 7. Contingency Reserves. An IH shall provide annually a reserve for contingencies in such reasonable amount as may be required by the Commission.

Sec. 8. Prohibitions

(1) No IH shall undertake underwriting commitments for its own account in an aggregate outstanding amount exceeding twenty (20) times its unimpaired capital and surplus.

(2) An IH shall not at any time allow its unimpaired capital and surplus to fall below ₱20.0 million; otherwise, it shall be prohibited from underwriting securities for so long as such deficiency remains.

(3) Whenever an IH is engaged in the management of funds, its officers and other personnel directly involved in the management of funds are prohibited from simultaneously or concurrently buying or selling the shares of stock of the same firm that the funds are buying or selling.

(4) No advance to directors, officers and stockholders owning at least 10% of the outstanding capital of an IH shall be allowed, unless sufficiently collateralized.

Sec. 9. Reporting Requirements. Every registered IH shall file with the Commission the following periodic reports in triplicate:

A. *Progress Reports* - a quarterly report of the results of its underwriting operations and activities of funds managed on all commitments entered into in such form as may be provided for the purpose, within fifteen (15) days from the end of each quarter.

B. *Semi-Annual Financial Statement* signed under oath by its chief accountant and verified by the president, within a period of sixty (60) days after the end of each semester containing such data, and in such form as the Commission shall require. A copy shall be filed with the BSP.

C. *Annual Report* concerning its operational activities for the year just ended, signed by its president (SEC Form 129-1) within the month of March of each year. A copy shall be filed with the BSP.

D. A *Report* on the composition of the board of directors or any resignation, dismissal, suspension, or filling of vacancies therein, or of any officers or managerial staff, signed under oath by the secretary, within fifteen (15) days after occurrence of the event.

Every registered IH shall maintain and preserve such records and documents as the Commission may prescribe by way of circulars. Such circulars shall provide for a reasonable degree of uniformity in accounting policies and principles to be followed by IHs in maintaining their accounting records and in preparing statements as required by these rules.

Sec. 10. Transitory Provisions

A. All existing enterprises which have been operating as Investment Houses, prior to 15 February 1973, shall:

(1) Within six (6) months from 15 February 1973 file an information sheet with the Commission in such form and containing such data as may be required, pay the required fee under Sec. 3-E of these rules, and the Commission in consultation with the Monetary Board, after determining compliance with the requirements of P.D. No. 129 and of these Rules, shall issue a License to Operate an IH.

(2) Within one (1) Year from 15 February 1973 comply with the requirement of a minimum paid-in capital of ₱20.0 million, citizenship requirements, and the prohibition on interlocking directorate or officership.

Sec. 11. Stockbrokerage or Dealership Functions. If an IH engages in the business of a stockbroker or dealer pursuant to P.D. No. 129, it shall comply with the provisions of C.A. No. 83, otherwise known as the Securities Act, and the rules and regulations of the Commission promulgated pursuant thereto: *Provided, however*, that an IHe need not obtain a separate license under Section 14 of the Securities Act.

Sec. 12. Bangko Sentral Rules. IHs shall also be subject to the rules and regulations promulgated by the BSP for non-bank financial intermediaries as provided by law.

Sec. 13. Visitorial Power. The Commission may, at its discretion, make such investigations as it deems necessary to determine whether or not an IH is complying with any of the provisions of P.D. No. 129 or of any applicable laws, rules and regulations. It shall determine all the facts and circumstances concerning the matter to be investigated for the imposition of sanctions/penalties or remedial or preventive measures.

Sec. 14. General Exemption Power The Commission may, upon proper petition and payment of a fee of ₱100, grant an exemption from compliance with any requirements of these rules as may be consistent with public interest and the protection of investors.

Sec. 15. Penalties. Any violation of P.D. No. 129 or of these rules and regulations, shall be penalized by suspension or revocation of the License to Operate, after proper notice and hearing. In appropriate cases, a fine not exceeding ₱200 per day for every day during which such violation continues, shall be imposed upon the IH and the officer or director who ordered or authorized the violation, without prejudice to the criminal liabilities provided in the second paragraph of Section 16 of P. D. No. 129.

In the exercise of its regulatory powers under Section 12 of P.D. No. 129, the Monetary Board may issue a cease-and-desist order upon an IH which is not complying with BSP rules and regulations pertaining to non-bank financial intermediaries or, in appropriate cases, rules governing quasi-banking functions of IHs. Failure to comply with the cease-and-desist order shall subject an IH to a fine to be imposed by the Monetary Board.

Sec. 16. Effectivity. These rules shall take effect immediately. They shall be published in a newspaper of general circulation in the Philippines and in the Official Gazette.

Manila, Philippines, 09 July 1973.

(SGD.) ARCADIO E. YABYABIN
Securities and Exchange Commissioner

APPROVED:

(SGD.) TROADIO T. QUIAZON, JR.
Acting Secretary of Trade

Date: 13 July 1973

Republic of the Philippines
Department of Finance
SECURITIES AND EXCHANGE COMMISSION
SEC Building, EDSA, Greenhills
Mandaluyong, Metro Manila

NEW RULES AND REGULATIONS TO IMPLEMENT THE PROVISIONS OF REPUBLIC ACT (R.A.) NO. 5980 (THE FINANCING COMPANY ACT), AS AMENDED

[Appendix to Sec. 4106Q (2008 - 4656Q)]

To effectively carry out the provisions of R.A. No. 5980 (The Financing Company Act), as amended, the Securities and Exchange Commission, pursuant to the powers vested in it under said Act, R.A. No. 1143 and Presidential Decree No. 902-A, as amended, hereby promulgates the following rules and regulations:

Section 1. Definition of Terms. The following definition of terms shall apply for purposes of these Rules:

a. FINANCING COMPANIES are corporations or partnerships, except those supervised by the Central Bank of the Philippines, Office of the Insurance Commissioner and the Bureau of Cooperatives Development, which are primarily organized for the purpose of extending credit facilities to consumers and to industrial, commercial, or agricultural enterprises: by discounting or factoring commercial papers or accounts receivable; by buying and selling contracts, leases, chattel mortgages, or other evidences of indebtedness; or by leasing of motor vehicles, heavy equipment and industrial machinery, business and office machines and equipment, appliances and other movable property.

b. PRIMARILY ORGANIZED shall mean organized for the primary purpose of operating as a financing company and that more than 50% of its funds shall be used or invested in financing company activities, *Provided, That* in the computation thereof direct loans and temporary investments in government securities shall be taken into account.

c. FUNDS as used herein shall mean total assets inclusive of allowance for doubtful accounts and deferred income less investment in real estate, shares of stock in a real estate development corporation and real estate based projects which shall not exceed 25% of networth of the investing company, leasehold rights and improvements, fixed assets inclusive of appraisal surplus, foreclosed properties and prepayments.

d. COMMISSION shall mean the Securities and Exchange Commission.

e. CREDIT shall mean any loan, mortgage, deed of trust, advance or discount, any conditional sales contract, any contract to sell, or sale or contract of sale of property or service, either for present or future delivery, under which, part or all of the price is payable subsequent to the making of such sale or contract, any rental-purchase contract, any option, demand, lien, pledge, or other claim against, or for the delivery of, property or money, any purchase, or other acquisition of or any credit upon the security of any obligation or claim arising out of the foregoing; and any transactions having a similar purpose or effect.

f. PURCHASE DISCOUNT is the difference between the value of the receivables purchased or credit assigned, and the net amount paid by the finance company for such purchase or assignment, exclusive of fees, service charges, interest and other charges incident to the extension of credit.

g. RECEIVABLES FINANCING is a mode of extending credit through the purchase by, or assignment to, a financing company of evidences of indebtedness or open accounts by the discounting or factoring.

h. DISCOUNTING is a type of receivables financing whereby evidences of indebtedness of a third party, such as installments contracts, promissory notes, and similar instruments, are purchased by, or assigned to, a financing company in an amount or for a consideration less than their face value.

i. FACTORING is a type of receivables financing whereby open accounts, not evidenced by a written promise to pay supported by documents such as but not limited to invoices of manufacturers and suppliers, delivery receipts and similar documents, are purchased by, or assigned to, a financing company in an amount or for a consideration less than the outstanding balance of the open accounts.

j. LEASING shall refer to the financial leasing which is a mode of extending credit through a non-cancellable contract under which the lessor purchases or acquires at the instance of the lessee heavy equipment, motor vehicles, industrial machinery, appliances, business and office machines, and other movable property in consideration of the periodic payment by the lessee of a fixed amount of money sufficient to amortize at least 70% of the purchase price or acquisition cost, including any incidental expenses and a margin of profit, over the lease period. The contract shall extend over an obligatory period during which the lessee has the right to hold and use the leased property and shall bear the cost of repairs, maintenance, insurance and preservation thereof, but with no obligation or option to the part of the lessee to purchase the leased property at the end of the lease contract.

k. PAID-UP CAPITAL refers to the amount paid for the subscription of stock in a corporation including the amount paid in excess of par value, while CAPITAL CONTRIBUTION refers to the total contributions of the partners in a partnership.

l. NETWORTH is the excess of assets over liabilities, net of appraisal surplus, and booked valuation reserves, capital adjustments, overstatement of assets and unrecorded liabilities.

Sec. 2. Form of Organization. Financing companies shall be organized in the form of: stock corporations in accordance with the provisions of the Corporation Code of the Philippines (Batas Pambansa Blg. 68) or general partnerships pursuant to the provisions of the New Civil Code of the Philippines and subject to the following:

a. At least sixty percentum (60%) of the outstanding capital stock of the corporation, and in case of a partnership, at least sixty percentum (60%) of the total capital contributions of the partners, shall be owned by citizens of the Philippines.

b. A minimum paid-up capital, in case of corporations, and capital contribution in case of partnerships, that shall maintain their principal offices in the areas hereunder specified, shall be made in cash or in property of at least:

1)	₱10,000,000	- Metro Manila Area
2)	5,000,000	- First Class Cities outside Metro Manila
3)	2,500,000	- Second Class Cities and First Class Municipalities

4)	1,000,000 -	Third Class Cities and Second Class Municipalities
5)	500,000 -	Fourth Class Cities, Third Class Municipalities and below

In case the area where the principal office of a financing company is located has been upgraded, the corresponding increase in capitalization requirement shall be undertaken within such period as the Commission shall fix.

Unless otherwise authorized by the Commission, all financing companies with a paid-up capital or capital contribution less than that mentioned above shall be given five (5) years within which to build up their capital requirement according to the following schedule:

	Metro Manila Area	1st Class Cities Out side Metro Manila	3rd Class 2nd Class Cities & 1st Class Municipalities	Cities & 2nd Class Municipalities
6-30-92	2,000,000	1,000,000	500,000	500,000
6-30-93	4,000,000	2,000,000	1,000,000	625,000
6-30-94	6,000,000	3,000,000	1,500,000	750,000
6-30-95	8,000,000	4,000,000	2,000,000	875,000
6-30-96	10,000,000	5,000,000	2,500,000	1,000,000

Any existing and/or new branch, agency, extension office or unit may operate subject to the provision of Section 5 thereof.

c. At least two-thirds of all the members of the board of directors in the case of a corporation and all the managing partners in case of a partnership shall be citizens and residents of the Philippines.

Any change in the membership in, or composition of, the board of directors, officers from the rank of VP and up or their equivalent, branch manager, cashier and administrative officer, or in the managing partners, as the case may be, shall be reported to the Commission within seven (7) working days thereafter, and the requirement prescribed under Section 3.a.4 and 7 and Section 5.a.3. and 4 hereof, shall be submitted within thirty (30) working days from date of the aforesaid change..

d. The corporate/partnership name of financing companies shall contain the term "financing company","finance company", or "finance and investment company" or other title or word(s) descriptive of its operations and activities as a financing company.

Sec. 3. Requirements for Registration

a. *Registration papers to be submitted to the Commission* - Any corporation or partnership may be registered as a financing company by filing with the Commission in five (5) copies an application to operate as a financing company under R.A. No. 5980, as amended, signed under oath by its President/Managing Partner, together with the following documents in the prescribed forms:

1) All documents required for registration as a corporation or partnership;

2) By-laws;

3) Information Sheet of registrant company;

4) Personal Information Sheet of each of the directors, officers with the rank of Vice-President and up or their equivalent or managing partners;

5) Answers to the questionnaire of the Commission;

6) Projected balance sheet, income statement and cash flow statement for three (3) years, together with a schedule of discounting, factoring, leasing and other financing activities and all related income therefrom.

7) Documents required of each director, officer to be appointed from the rank of Vice-President and up or their equivalent, or managing partner such as the following:

a) Police clearance from local police of the city or municipality of which he is a resident;

b) NBI clearance;

c) Certificate of good moral character to be executed under oath by at least two (2) reputable and disinterested persons in the community;

d) Bank credit information to be issued by his depository or creditor bank(s), if any; and

8) Such other documents as may be required by the Commission whenever it deems necessary.

b. *Publication and Posting of Notice and Order for Registration* - Upon receipt of the above registration papers of a proposed financing company, the Commission shall cause the notice and order to be published by the applicant company at its expense in a newspaper of general circulation in the Philippines once a week for two (2) consecutive weeks, and the notice shall simultaneously be posted in a public and conspicuous place where the principal office of the company will be located and in the Office of the Commission for the same period.

The notice shall state, among others, the name of the proposed financing company, the capital structure in case of a corporation or the total capital contribution in case of a partnership, and the names and residences of its directors or managing partners.

c. *Opposition to Registration, if any* - Any interested party may oppose the registration of a financing company in writing, personally or through counsel, within fifteen (15) days after the last date of the publication of the notice. If after the hearing, the Commission finds that the requirements of R. A. No. 5980, as amended, its implementing rules and regulations and other pertinent laws have been complied with and that no valid reason exists for the disapproval of the application, the Commission shall take appropriate action on said application.

Sec. 4. Issuance of Certificate of Filing of Articles of Incorporation and By-Laws; Certificate of Authority; Conditions for Commencement of Operations

a. The Commission, in consultation with the Central Bank, shall register the articles of incorporation and by-laws or articles of partnership of, and issue the Certificate of Authority to Operate to, any proposed financing company if it is satisfied that the establishment of such company will promote public interest and convenience, and on the basis of the documents and/or evidences submitted, that;

1) All the requirements of R. A. No. 5980, as amended, other existing laws, and applicable rules and regulations to engage in the business for which the applicant is proposed to be incorporated, or organized, have been complied with;

2) The organization, direction and administration of the applicant, as well as the integrity and responsibility of the organizers and administrators, presumably assure the protection of the interest of the general public; and

3) Proof of the publication and posting of the notice and order for registration is in accordance with Sec. 3.b. hereof.

b. A corporation or partnership which has been duly registered, and granted a Certificate of Authority to Operate as a financing company in accordance with the law and these Rules, shall commence operations within ninety (90) days from date of grant of such certificate. Failure to operate within the prescribed ninety (90) days period shall subject the financing company to a fine of not less than One Thousand (₱1,000.00) Pesos unless its non-operation is reasonably justified, as determined by the Commission.

c. The financing company may be granted a grace period of another ninety

(90) days from the expiry date of the first ninety (90) days within which to commence operations notwithstanding its failure to operate as aforestated. Failure to operate within the extended period shall empower the Commission, after notice and hearing, to revoke its Certificate of Authority.

Sec. 5. Branches, Agencies, Extension Offices or Units

a. *Certificate of Authority* - No financing company shall establish or operate a branch, agency, extension office or unit without a prior certificate of authority to be issued by the Commission. The application for authority filed under this section shall be accompanied by the following documents:

1) Information Sheet of the proposed branch;

2) Answer to SEC questionnaire;

3) Police clearance of the manager, cashier, and administrative officer of the proposed branch;

4) NBI clearance of the branch manager, cashier and administrative officer of the proposed branch;

5) Copy of the proposed personnel chart; and

6) Such other documents as may be required by the Commission whenever it deems necessary.

The above application shall be published in accordance with the provisions of Sec. 3.b. of these Rules. However, the Notice and Order shall be posted in a public and conspicuous place where the aforesaid branch, agency, extension office or unit shall be established.

b. *Evaluation Guideposts* - The number of branches, agencies, extension offices or units to be established shall depend upon the capacity of the company to conduct expanded operations and/or upon the capacity of the area wherein the proposed branch, extension office, agency or unit will be established, to absorb new entities engaged in financing, as may be determined by the Commission.

c. *Additional Capital Requirement* - A financing company may be required to put up additional capital for branches, agencies, extension offices or units in an amount to be determined by the Commission.

d. *Prescribed Period to Operate* - Such branch, agency, extension office or unit shall operate within ninety (90) days from the issuance of the certificate of authority and failure to operate within such period shall subject said branch, agency, extension office or unit to a fine of not less than One Thousand (₱1,000) Pesos or revocation of the certificate of authority, after due hearing at the discretion of the Commission, unless its non-operation is reasonably justified as determined by the Commission.

e. *Term of Authority to Operate* - The certificate of authority to operate a branch, agency, extension office or unit shall be co-terminus with that of the head office.

Sec. 6. Applicability of Central Bank Regulations - Financing companies duly licensed to operate as such, their branches, agencies, extension offices or units shall also be subject to applicable Central Bank regulations.

Sec. 7. Licensing Fees - A fee of 1/10 of 1% of the minimum paid-up capital or capital contribution required under Section 2.b. shall be charged for the issuance of the Certificate of Authority to Operate as a financing company.

A fee of one-tenth of one percent (1/10 of 1%) of the additional required capital under Sec. 5.c., but in no case less than ₱250.00 shall be charged likewise for the issuance of original Certificate of Authority of each branch, agency, extension office or unit of such financing company.

Sec. 8. Loans and Investments

a. Financing companies may engage in direct lending if authorized by the secondary purposes in its articles of incorporation and in accordance with Section 42 of the Corporation Code of the Philippines (B.P. 68).

b. Unless otherwise authorized by the Commission, the total investment in real estate and in shares of stock in a real estate development corporation and other real estate based projects shall not at any time exceed twenty-five (25%) per cent of the net worth of the investing financing company.

Sec. 9. Conveyance of Evidences of Indebtedness and Financed Receivables

a. The negotiation, sale or assignment by financing companies of evidences of indebtedness shall be in accordance with the rules of the Commission on registration of commercial papers.

b. Accounts which have been factored or discounted by, the lease receivables of, and other evidences of indebtedness (not covered in Item a. above) issued or negotiated to, a financing company shall not be sold, assigned or transferred in any manner except to banks including their trust accounts, trust companies, QBs, investment houses including their trust accounts, financing companies, investment companies, NSSLAs, insurance companies, government FIs, pension and retirement funds approved by the Bureau of Internal Revenue, educational assistance funds established by the National Government; *Provided, That* the negotiation of evidence of indebtedness to pension funds or educational assistance funds shall be on a recourse basis.

Sec. 10. Other Activities

a. Financing companies not duly authorized to perform quasi-banking functions shall not act as dealers in commercial papers but may act as dealers in other securities provided they are duly licensed by the Commission as such.

b. Financing companies shall not act as dealers of certificates of time deposit.

c. Except in cases of issuances to primary institutional lenders, financing companies without quasi-banking license shall not issue instruments other than promissory notes, to cover placements with, or borrowing by, them.

Sec. 11. Purchase Discount/Fees/Service and Other Charges - The purchase discounts, fees, service and other charges of financing companies on assignments of credit, purchases of installment papers, accounts receivable or other evidences of indebtedness, factoring of accounts receivable or other evidences of indebtedness, or leasing transactions shall be in accordance with the rules prescribed by the Monetary Board, in consultation with the Commission, pursuant to the provisions of Section 5 of R.A. No. 5980, as amended by P.D. No. 1454.

Sec. 12. Networth for Operating Financing Companies - The company's networth shall be maintained at an amount not less than that required under Sections 2.b. and 5.c. hereof.

Sec. 13. Prohibitions

a. No corporation shall be allowed to include financing activities as herein defined as one of its secondary purposes.

b. No person, association, partnership or corporation shall do or hold itself out as doing business as a financing company or finance and investment company or under any other title or name tending to give the public the impression that it is a financing company unless so authorized under R. A. No. 5980, as amended.

Sec. 14. Periodic Reports - Every financing company shall file with the Commission the following quarterly reports: a) Statement of Condition and Statement of Income and Expenses, together with the schedule of aging of receivables (indicating the maturity pattern of the aforesaid receivables under due within 1 year, due over 1 year to be applicable to long term receivables only, past due accounts to subdivided further to past due accounts within 1 year, over 1 year and litigation items), payable (indicating likewise the same maturing pattern of within 1 year and over 1 year) and off-balance sheet items; *Provided, however*, That respective collateral/s (if any) for past due accounts over 1 year and litigation items shall be adequately disclosed in the aforementioned Schedules and b) list of officers, directors, and stockholders. These reports shall be signed under oath by the company's principal executive officer and principal financial officer and shall be submitted within thirty (30) calendar days after the end of each quarter. They shall, likewise, file four (4) copies of their audited financial statements within 120 days after the end of their fiscal years and such other reports as may be required by the Commission.

Sec. 15. Administrative Sanctions - If the Commission finds that there is a violation of these Rules and Regulations and their implementing circulars or any of the terms and conditions of the Certificate of Authority to operate as a financing company, or any Commission order, decision or ruling, or refuses to have its books of accounts audited, or continuously fail to comply with SEC requirements, the Commission shall, in its discretion, impose any or all of the following sanctions:

a. Suspension or revocation of the certificate of authority to operate as a financing company after proper notice and hearing;

b. A fine in accordance with the guidelines that the Commission shall issue from time to time;

c. Other sanctions within the power of the Commission and the Central Bank under existing laws.

The imposition of the foregoing administrative sanctions shall not preclude the institution of appropriate action against the officers and directors of the financing company or any person who might have participated therein, directly or indirectly, in violation of R. A. No. 5980, as amended, and these Rules and Regulations.

Sec. 16. Cease and Desist Order - The Commission may, on its own motion or upon verified complaint of any aggrieved party, issue a Cease and Desist Order *ex-parte*, if the violation(s) mentioned in the preceding sections may cause grave or irreparable injury to the public or may amount to culpable fraud or violation of these Rules and Regulations, implementing circulars, certificates of authority issued by the Commission, or of any order, decision or ruling thereof.

The issuance of such Cease and Desist Order automatically suspends the authority to operate as a financing company.

Immediately upon the issuance of an *ex-parte* Cease and Desist Order, the Commission shall notify the parties involved and schedule a hearing on whether to lift such order or to impose administrative sanctions provided for in Section 16 not later than fifteen (15) days after service of notice.

Sec. 17. Transitory Provision - Any corporation/partnership at the time of the effectivity of these Rules has been registered and licensed by the Commission to operate as a financing company, shall be considered as registered and licensed under the provisions of these Rules, subject to the terms and conditions of the license,

and shall be governed by the provisions hereof; *Provided, however*, That financing companies with existing certificate of authority shall surrender the same to the Commission upon payment of the annual fee pursuant to Section 7 hereof to be replaced by new certificate of authority and, *Provided,* That where such corporation/ partnership is affected by the new provisions hereof, said corporation/ partnership shall, unless otherwise herein provided, be given a period of not more than one (1) year from the effectivity of these Rules within which to comply with the same.

Sec. 18. Effectivity - These Rules and Regulations shall take effect fifteen (15) days after publication in two (2) newspapers of general circulation in the Philippines.

Mandaluyong, Metro Manila, Philippines
16 October 1991.

(SGD.) ROSARIO N. LOPEZ
Chairman
Securities and Exchange Commission

CLASSIFICATION, ACCOUNTING PROCEDURES, VALUATION AND SALES AND TRANSFERS OF INVESTMENTS IN DEBT SECURITIES AND MARKETABLE EQUITY SECURITIES

[Appendix to Subsec. 4388Q.5 (2008 - 4391Q.3)]

Section 1. Statement of Policy. It is the policy of the BSP to promote full transparency of the financial statements of banks and other supervised institutions in order to strengthen market discipline, encourage sound risk management practices, and stimulate the domestic capital market. Towards these ends, the BSP desires to align local financial accounting standards with international accounting standards as prescribed by the International Accounting Standards Board (IASB) to the greatest extent possible.

Sec. 2. Scope. This Appendix covers accounting for investments in debt and equity securities except:

a. those that are part of hedging relationship;

b. those that are hybrid financial instruments;

c. those financial liabilities that are held for trading;

d. those financial assets and financial liabilities which, upon initial recognition, are designated by the FIs as at fair value through profit or loss; and

e. those that are classified as loans and receivables.

It also does not include accounting for derivatives and non-derivative financial instruments other than debt and equity securities. The foregoing exceptions and exclusions shall be covered by separate regulations.

Sec. 3. Investments in Debt and Equity Securities. Depending on the intent, investments in debt and equity securities shall be classified into one (1) of four (4) categories and accounted for as follows[1]:

a. Held to Maturity (HTM) Securities - These are debt securities with fixed or determinable payments and fixed maturity that an FI has the positive intention and ability to hold to maturity other than:

(1) those that meet the definition of Securities at Fair Value Through Profit or Loss; and

(2) those that the FI designates as ASS.

An FI shall not classify any debt security as HTM if the FI has, during the current financial year or during the two (2) preceding financial years, sold or reclassified more than an insignificant amount of HTM investments before maturity (more than insignificant in relation to the total amount of HTM investments) other than sales or reclassifications that:

(a) are so close to maturity or the security's call date (i.e., less than three (3) months before maturity) that changes in the market rate of interest would not have a significant effect on the security's fair value;

(b) occur after the FI has substantially collected all [i.e., at least eighty-five percent (85%)] of the security's original principal through scheduled payments or prepayments; or

(c) are attributable to an isolated event that is beyond the FI's control, is non-recurring and could not have been reasonably anticipated by the FI.

For this purpose, the phrase *"more than an insignificant amount"* refers to sales or reclassification of one percent (1%) or more of the outstanding balance of the HTM portfolio: *Provided, however,* That sales or reclassifications of less than one percent (1%) shall be evaluated on case-to-case basis.

[1] Reclassification allowed until 30 November 2005 as per MAB dated 23 November 2005

Sales or reclassifications before maturity that do not meet any of the conditions prescribed in this Appendix shall require the entire HTM portfolio to be reclassified to ASS. Further, the FI shall be prohibited from using the HTM account during the reporting year of the date of sales or reclassifications and for the succeeding two (2) full financial years. Failure to reclassify the HTM portfolio to ASS on the date of sales or reclassifications, shall subject the FI and concerned officers to penalties and sanctions provided under 4388Q.5. This provision shall be applied prospectively, i.e., on prohibited sales or reclassifications occurring from 13 March 2005 (effectivity date of Circular No. 476 dated 16 February 2005) and thereafter.

Securities held in compliance with BSP regulations, e.g., securities held as liquidity reserves and for the faithful performance of trust duties, may be classified either as HTM, Securities Held for Trading (HFT) or ASS: *Provided*, That the provision of Item *(4)* of paragraph 2 of Section 3.a.1 shall not apply to sales or reclassifications of the said securities booked under HTM.

a.1.Positive intention and ability to hold investments in HTM securities to maturity - An FI does not have a positive intention to hold to maturity an HTM security if:

(a) the FI intends to hold the security for an undefined period;

(b) the FI stands ready to sell the security (other than if a situation arises that is non-recurring and could not have been reasonably anticipated by the FI) in response to changes in market interest rates or risks, liquidity needs, changes in the availability of and the yield on alternative investments, changes in financing sources and terms or changes in foreign currency risk; or

(c) the issuer has a right to settle the security at an amount significantly below its amortized cost.

Sales before maturity could satisfy the condition of HTM classification and therefore need not raise a question about the FI's intention to hold other HTM securities to maturity if they are attributable to any of the following:

(i) A significant deterioration in the issuer's creditworthiness; for example, a sale following a downgrade in a credit rating by an external rating agency would not necessarily raise a question about the FI's intention to hold other investments to maturity if the downgrade provides evidence of a significant deterioration in the issuer's creditworthiness judged by reference to the credit rating at initial recognition. Similarly, if an FI uses internal ratings for assessing exposures, changes in those internal ratings may help to identify issuers for which there has been a significant deterioration in creditworthiness, provided the FI's approach to assigning internal ratings and changes in those ratings give a consistent, reliable and objective measure of the credit quality of the issuers. If there is evidence that an instrument is impaired, the deterioration in creditworthiness is often regarded as significant.

(ii) A change in tax law that eliminates or significantly reduces the tax-exempt status of interest on the HTM security (but not a change in tax law that revises the marginal tax rates applicable to interest income);

(iii) A major business combination or major disposition (such as sale of a segment) that necessitates the sale or transfer of HTM securities to maintain the FI's existing interest rate risk position or credit risk policy: *Provided*, That the sale or transfer of HTM security shall be done only once and within a period of six (6) months from the date of the business combination or major disposition: *Provided, further*, That prior BSP approval is required for sales or transfers occurring after the prescribed six (6)-month time frame. In this case, FIs shall submit to the appropriate department of the SES, a plan stating the reason for the

extension and the proposed schedule for the disposition of the HTM security.

(iv) A change in statutory or regulatory requirements significantly modifying either what constitutes a permissible investment or the maximum level of particular types of investments, thereby causing an FI to dispose of an HTM security;

(v) A significant increase in the industry's regulatory capital requirements that causes the FI to downsize by selling HTM securities; or

(vi) A significant increase in the risk weights of HTM securities used for regulatory risk-based capital purposes.

An FI does not have a demonstrated ability to hold to maturity an investment in HTM security if:

(aa) it does not have the financial resources available to continue to finance the investment until maturity; or

(bb) it is subject to an existing legal or other constraint that could frustrate its intention to hold the security to maturity.

Sales before maturity due to events that are non-recurring and could not have been reasonably anticipated by the FI such as a run on a bank, likewise satisfy the condition of HTM classification and therefore need not raise a question about the FI's intention and ability to hold other HTM investments to maturity.

An FI assesses its intention and ability to hold its investment in HTM securities to maturity not only when those securities are initially recognized, but also at each time that the FI prepares its financial statements.

a.2. HTM securities shall be measured upon initial recognition at their fair value plus transaction costs that are directly attributable to the acquisition of the securities.

For this purpose, *transactions costs* include fees and commissions paid to agents (including employees acting as selling agents), advisers, brokers and dealers, levies by regulatory agencies and securities exchanges, and transfer taxes and duties. Transaction costs do not include debt premiums or discounts, financing costs or internal administrative or holding costs.

After initial recognition, an FI shall measure HTM securities at their amortized cost using the effective interest method.

For this purpose, the *effective interest method* is a method of calculating the amortized cost of a security (or group of securities) and of allocating the interest income over the relevant period using the effective interest rate. The *effective interest rate* shall refer to the rate that exactly discounts the estimated future cash receipts through the expected life of the security or when appropriate, a shorter period to the net carrying amount of the security. When calculating the effective interest rate, an FI shall estimate cash flows considering all contractual terms of the security (for example, prepayment, call and similar options) but shall not consider future credit losses. The calculation includes all fees and points paid to the other party to the contract that are an integral part of the effective interest rate, transaction costs, and all other premiums or discounts. There is a presumption that the cash flows and the expected life of a group of similar securities can be estimated reliably. However, in those rare cases when it is not possible to estimate reliably the cash flows or the expected life of a security (or group of securities), the FI shall use the contractual cash flows over the full contractual terms of the security.

A gain or loss arising from the change in the fair value of the HTM security shall be recognized in profit or loss when the security is derecognized or impaired, and through the amortization process.

An FI shall assess at each time it prepares its financial statements whether there is any objective evidence that an HTM security is impaired.

If there is objective evidence that an impairment loss on HTM securities has been

incurred, the amount of the loss is measured as the difference between the security's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the security's original effective interest rate (i.e. the effective interest rate computed at initial recognition). The carrying amount of the security shall be reduced through the use of an allowance account. The amount of the loss shall be recognized in profit or loss.

As a practical expedient, a creditor may measure impairment of HTM securities on the basis of an instrument's fair value using an observable market price.

An FI first assesses whether objective evidence of impairment exists individually for HTM securities that are individually significant, and individually or collectively for HTM securities that are not individually significant. If an entity determines that no objective evidence of impairment exists for an individually assessed HTM security, whether significant or not, it includes the asset in a group of HTM securities with similar credit risk characteristics and collectively assesses them for impairment. HTM securities that are individually assessed for impairment and for which an impairment loss is or continues to be recognized are not included in a collective assessment of impairment.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognized (such as an improvement in the debtor's credit rating), the previously recognized impairment loss shall be reversed by adjusting the allowance account. The reversal shall not result in a carrying amount of the security that exceeds what the amortized cost would have been had the impairment not been recognized at the date the impairment is reversed. The amount of the reversal shall be recognized in profit or loss.

b. Securities at Fair Value through Profit or Loss - These consist initially of HFT securities. HFT are debt and equity securities that are:

(1) acquired principally for the purpose of selling or repurchasing them in the near term; or

(2) part of a portfolio of identified securities that are managed together and for which there is evidence of a recent actual pattern of short-term profit-taking.

For this purpose, an FI shall adopt its own definition of short-term which shall be within a (twelve) 12-month period. Said definition which shall be included in its manual of operations, shall be applied and used consistently.

b.1 HFT securities shall be measured upon initial recognition at their fair value. Transaction costs incurred at the acquisition of HFT securities shall be recognized directly in profit or loss. After initial recognition, an FI shall measure HFT securities at their fair values without any deduction for transaction costs that it may incur on sale or other disposal. A gain or loss arising from a change in the fair value of HFT securities shall be recognized in profit or loss under the account "Trading Gain/(Loss)".

c. ASS. These are debt or equity securities that are designated as Available-for- Sale or are not classified/designated as (a) HTM, (b) Securities at Fair Value through Profit or Loss, or (c) Investment in Non-Marketable Equity Securities (INMES).

c.1 ASS shall be measured upon initial recognition at their fair value plus transaction costs that are directly attributable to the acquisition of the securities. After initial recognition, an FI shall measure ASS at their fair values, without any deduction for transaction costs it may incur on sale or other disposal. A gain or loss arising from a change in the fair value of an ASS shall be recognized directly in equity under the account "Net

Unrealized Gains/(Losses) on Securities Available-for-Sale" and reflected in the statement of changes in equity, except for impairment losses and FX gains and losses, until the security is derecognized, at which time the cumulative gain or loss previously recognized in equity shall be recognized in profit or loss. However, interest calculated using the effective interest method is recognized in profit or loss. Dividends on an Available- for- Sale equity security are recognized in profit or loss when the FI's right to receive payment is established.

For the purpose of recognizing foreign exchange gains and losses on a monetary ASS that is denominated in a foreign currency, it shall be treated as if it were carried at amortized cost in the foreign currency. Accordingly, for such an ASS, exchange differences resulting from changes in amortized cost are recognized in profit or loss and other changes in carrying amount are recognized directly in equity. For ASS that are not monetary items (for example, equity instruments), the gain or loss that is recognized directly in equity includes any related foreign exchange component.

An FI shall assess at each time it prepares its financial statements whether there is any objective evidence that an ASS is impaired.

When a decline in the fair value of an ASS has been recognized directly in equity and there is objective evidence that the asset is impaired, the cumulative loss that had been recognized directly in equity shall be removed from equity and recognized in profit or loss even though the security has not been derecognized.

The amount of the cumulative loss that is removed from equity and recognized in profit or loss shall be the difference between the acquisition cost (net of any principal repayment and amortization) and current fair value, less any impairment loss on that security previously recognized in profit or loss.

Impairment losses recognized in profit or loss for an investment in an equity instrument classified as Available-for-Sale shall not be reversed through profit or loss.

If, in a subsequent period, the fair value of a debt instrument classified as Available-for-Sale increases and the increase can be objectively related to an event occurring after the impairment loss was recognized in profit or loss, the impairment loss shall be reversed, with the amount of the reversal recognized in profit or loss.

c.2. Underwriting Accounts (UA) shall be a sub-account under Available-for-Sale. These are debt and equity securities purchased which have remained unsold/ locked-in from underwriting ventures on a firm basis. UA account is applicable only to UBs and IHs.

d. INMES - These are equity instruments that do not have a quoted market price in an active market, and whose fair value cannot be reliably measured.

INMES shall be measured upon initial recognition at its fair value plus transaction costs that are directly attributable to the acquisition of the security. After initial recognition, an FI shall measure INMES at cost. A gain or loss arising from the change in fair value of the INMES shall be recognized in profit or loss when the security is derecognized or impaired.

An FI shall assess each time it prepares its financial statements whether there is any objective evidence that an INMES is impaired.

If there is objective evidence that an impairment loss has been incurred on an INMES, the amount of impairment loss is measured as the difference between the carrying amount of the security and the estimated future cash flows discounted at the current market rate of return for a similar

financial instrument. Such impairment loss shall not be reversed.

For Securities at Fair Value through Profit or Loss and Available-for-Sale, an FI is required to book the mark-to-market valuation on a daily basis. However, an FI may opt to book the mark-to-market valuation every end of the month: *Provided*, That an adequate mechanism is in place to determine the daily fair values of securities.

An FI shall recognize an investment in debt or equity security on its balance sheet when, and only when, the FI becomes a party to the contractual provisions of the financial instrument. A regular way purchase or sale of financial assets shall be recognized and derecognized, as applicable using trade date accounting or settlement date accounting. The method used is applied consistently for all purchases and sale of financial assets that belong to the same category.

Sec. 4. Reclassifications[1]

a. An FI shall not reclassify a security into or out of the Fair Value through Profit Loss category while it is held.

b. If, as a result of a change in intention or ability, it is no longer appropriate to classify a debt security as HTM, it shall be reclassified as Available-for-Sale and remeasured at fair value, and the difference between its carrying amount and fair value shall be accounted for in accordance with Section 3.c.1.

c. Whenever sales or reclassifications of more than an insignificant amount of HTM investments do not meet any of the conditions in Section 3.a, any remaining HTM investments shall be reclassified as Available-for-Sale. On such reclassification, the difference between the carrying amount and fair value shall be accounted for in accordance with Section 3.c.1.

d. If a reliable measure becomes available for an INMES, it shall be reclassified as Available-for-Sale and remeasured at fair value, and the difference between its carrying amount and the fair value shall be accounted for in accordance with Section 3.c.1.

e. If, as a result of a change in intention or ability, or because the two (2) preceding financial years' referred to in Section 3.a have passed, it becomes appropriate to carry the debt security at amortized cost (i.e, HTM) rather than at fair value (i.e, Available-for-Sale), the fair value carrying amount of the security on that date becomes its new amortized cost. Any previous gain or loss on that debt security that has been recognized directly in equity in accordance with Section 3.c.1 shall be amortized to profit or loss over the remaining life of the HTM using the effective interest method. Any difference between the new amortized cost and maturity amount shall also be amortized over the remaining life of the security using the effective interest method, similar to the amortization of a premium and a discount. If the security is subsequently impaired, any gain or loss that has been recognized directly in equity is recognized in profit or loss in accordance with Section 3.c.1.

f. If, in the rare circumstance that a reliable measure of fair value is no longer available, it becomes appropriate to carry the equity security at cost (i.e, INMES) rather than at fair value (i.e, Available-for-Sale), the fair value carrying amount of the security on that date becomes its new cost. Any previous gain or loss on that equity security that has been recognized directly in equity in accordance with Section 3.c.1 shall remain in equity until the security is sold or otherwise disposed of, when it shall be recognized in profit or loss. If the financial asset is subsequently impaired, any previous

[1] The guidelines governing the reclassification of financial assets between categories in accordance with the provisions of the October 2008 amendments to PAS39 and PFRS7 are shown in Annex A.

gain or loss that has been recognized directly in equity is recognized in profit or loss in accordance with Section 3.c.1.

g. The following securities booked under the HTM category, shall be exempted from the "tainting" provision for prudential reporting purposes which prohibits FIs from using the HTM category and requires reclassification of the entire HTM portfolio to the Available-for-Sale category during the reporting year and for the succeeding two full financial years whenever an FI sells or reclassifies more than an insignificant amount of HTM investments before maturity, other than for reasons specified in Items *"a(a)"* to *"a(c)"* of Section 3 of this Appendix: *Provided,* That securities rejected under items *"i"* , *"ii"* and *"iii"* shall continue to be booked under the HTM category:

i. Securities exchanged pursuant to the Domestic Debt Exchange Offer of the Republic of the Philippines;

ii. Securities offered and accepted in the Global Bond Offering of the Republic of the Philippines;

iii. Securities offered and accepted in debt exchange offerings of GOCCs which carry the guarantee of the Philippine National Government, and

iv. Foreign currency denominated NG/BSP bonds/debt securities, outstanding as of 10 February 2007, which were reclassified from the HTM category in view of the increased risk-weights of said securities under *Appendix Q-46* within thirty (30) calendar days after 10 February 2007. The subject securities once reclassified shall be accounted for in accordance with the measurement requirements of their new category (i.e., ASS).

Sec. 5. Impairment. A debt or equity security is impaired and impairment losses are incurred if, and only if, there is objective evidence of impairment as a result of event that occurred after the initial recognition of the security (a "loss event") and that loss event has impact on the estimated future cash flows of the securities. Losses expected as a result of future events, no matter how likely, are not recognized. Objective evidence that the security is impaired includes observable data that comes to the attention of the holder of the security about the following loss events:

a. significant financial difficulty of the issuer or obligor;

b. a breach of contract, such as a default or delinquency in interest or principal payments;

c. the FI, for economic or legal reasons relating to the issuer's financial difficulty, granting to the issuer a concession that the FI would not otherwise consider;

d. it becoming probable that the issuer will enter bankruptcy or other financial reorganization;

e. the disappearance of an active market for that security because of financial difficulties; or

f. observable data indicating that there is a measurable decrease in the estimated future cash flows from a portfolio of securities since the initial recognition of those assets, although the decrease cannot yet be identified with the individual securities in the portfolio, including:

(1) adverse change in the payment status of issuers in the portfolio; or

(2) national or local economic conditions that correlate with defaults on the securities in the portfolio.

The disappearance of an active market because an FI's held securities are no longer publicly traded is not evidence of impairment. A downgrade of an issuer's credit rating is not, of itself, evidence of impairment, although it may be evidence of impairment when considered with other

available information. A decline in the fair value of a security below its cost or amortized cost is not necessarily evidence of impairment (for example, a decline in fair value of an investment in debt security that results from an increase in the risk free interest rate).

In addition to the types of events enumerated in Items "*a*" to "*f*" in this Section, objective evidence of impairment for an investment in an equity instrument includes information about significant changes with an adverse effect that have taken place in the technological, market, economic or legal environment in which the issuer operates and indicates that the cost of the investment in the equity instrument may not be recovered. A significant or prolonged decline in the fair value of an investment in an equity security below its cost is also objective evidence of impairment.

Sec. 6. Operations Manual. The FI shall maintain an operations manual for booking and valuation of HTM, Securities at Fair Value through Profit or Loss, Available for Sale and INMES.

(As amended by Circular Nos. 670 dated 18 November 2009, 628 dated 31 October 2008, 626 dated 23 October 2008, 558 dated 22 January 2007, 546 dated 21 September 2006 and 509 dated 01 February 2006)

Annex A

RECLASSIFICATION OF FINANCIAL ASSETS BETWEEN CATEGORIES

The following quidelines govern the reclassification of investments in debt and equity securities between categories:

Section I. Conditions for Reclassifications
FIs shall be allowed to reclassify their investments in debt and equity securities from the Held for Trading (HFT) or Available for Sale (AFS) categories to the Held to Maturity (HTM) or Unquoted Debt Securities Classified as Loans (UDSCL) categories, subject to the following conditions:

(1) The reclassification shall be done in accordance with the provisions of the October 2008 amendments to the International Accounting Standards (IAS) 39: *Financial Instruments: Recognition* and Measurements and International Financial Reporting Standards (IFRS) 7: Financial Instruments: *Disclosures;*

(a) Only non-derivative financial assets may be reclassified from HFT to AFS, HTM or UDSCL. This shall however exclude those that are Designated at Fair Value through Profit or Loss (DFVPL).

(b) A financial asset may be reclassified out of HFT into AFS/HTM/ UDSCL only in rare circumstances and if there is a change in intention (i.e., the financial asset is no longer held for the purpose of selling or repurchasing it in the near term). The financial assets shall be reclassified at their fair values on the effective date of reclassification all at the same time. Any gain or loss already recognized in profit or loss shall not be reversed. The fair value of a financial asset on the effective date of reclassification becomes its new cost or amortized cost, as applicable.

For this purpose, FIs may reclassify all or a portion of its financial assets for HFT to AFS/HTM/UDSCL as of the same date which shall be any day from 01 July 2008 to 14 November 2008. For example, an FI may choose to reclassify all financial assets booked under HFT to AFS/HTM/UDSCL as of 01 July 2008 using their fair values as of 01 July 2008. Another FI may choose to reclassify all financial assets booked under HFT to AFS/HTM/UDSCL as of 14 November 2008 using their fair values as of 14 November 2008. Thereafter, FIs shall not be allowed to "retrospectively" reclassify HFT to AFS/HTM/UDSCL. Any reclassification on or after 15 November 2008 shall take effect only from the date when the reclassification is made.

(c) A financial asset booked under HFT that would have also met the definition on UDSCL if the financial asset had not been required to be classified as HFT at initial recognition, may be reclassified from HFT to UDSCL if the entity has the intention and ability to hold the financial asset for the foreseeable future or until maturity.

(d) The financial assets shall be reclassified at their fair values on the effective date of reclassification, not necessarily all at the same time. Any gain or loss already recognized in profit or loss shall not be reversed. The fair value of a financial asset on the effective date of reclassification becomes its new cost or amortized cost, as applicable.

For this purpose, FIs may reclassify said financial assets from HFT to UDSCL as of any date from 01 July 2008 to 14 November 2008. Thereafter, FIs shall not be allowed to retrospectively reclassify HFT to UDSCL. Any reclassification on or

after 15 November 2008 shall take effect only from the date when the reclassification is made.

(e) The financial asset reclassified in accordance with *Items "(b)", "(c)"* or *"(d)"* above shall thereafter be treated in accordance with the guidelines provided in *Appendix 20: Provided, however,* That if an FI subsequently increases its estimates of future cash receipts as a result of increased recoverability of those cash receipts, the effect of that increase shall be recognized as an adjustment to the effective interest rate from the date of the change in estimate rather than as an adjustment to the carrying amount of the asset at the date of the change in estimate.

(f) FIs that shall reclassify based on the provision of this Annex shall comply with the disclosure requirements under the Amendments to IAS 39 and IFRS 7 in preparing their audited financial statements.

(2) Financial assets that are reclassified from HFT/AFS to HTM/ UDSCL shall thereafter be treated in accordance with the guidelines provided under *Appendix 33;*

(3) Reclassification from the AFS to the HTM category shall only be allowed if there was a change in intention for holding the debt instrument, and the financial institution has the ability to hold it until maturity; and

(4) FIs may reclassify from HFT/AFS to AFS/HTM/UDSCL effective 01 July 2008: *Provided,* That any reclassification made in periods beginning on or after 15 November 2008 shall take effect from the date when the reclassification is made.

Sec. II. Alternative accounting treatment for prudential reporting purposes. The following may be adopted for purposes of prudential reports:

(1) A financial asset booked under AFS may be reclassified from AFS to HTM/ UDSCL if the FI has the intention and ability to hold the financial assets for the foreseeable future or until the maturity using the fair value carrying amount of the financial assets as of the effective date of reclassification.

For this purpose, FIs may reclassify said financial assets from AFS to HTM/ UDSCL as of any day from 01 July 2008 to 14 November 2008. Thereafter, FIs shall not be allowed to retrospectively reclassify AFS to HTM/UDSCL. Any reclassification on or after 15 November 2008 shall take effect only from the date when ther reclassification is made.

(2) Financial assets that are booked under AFS category because of the tainting of the HTM portfolio may be reclassified to HTM or UDSCL using the fair value carrying amount of the financial assets as of the effective date of reclassification.

For this purpose, FIs may reclassify said financial assets from AFS to HTM/ UDSCL as of any day from 01 July 2008 to 14 November 2008.

(3) Hybrid financial assets (other than CLNs) may be included among the financial assets that may be reclassified out of the HFT and into the AFS/HTM/UDSCL in accordance with *Items "(1)(b)"* and *"(1)(c)"* in Sec. I by, first, bifurcating the embedded derivative from the host instrument and booking the derivatives under Derivatives with Positive/Negative Fair Value; and second, reclassifying the host contract to AFS/HTM/UDSCL.

(4) CLNs and other similar instruments that are linked to ROPs, on the other hand, may be included among the financial assets that may be reclassified (i) out of the HFT into AFS/HTM/UDSCL in accordance with *Items "(1)(b)"* and *"(1)(c)"*; or (ii) from AFS to UDSCL or HTM in accordance with *Item "(1)(d)"* all in Sec. I and *Item "1"* above, without bifurcating the embedded derivatives from the host instrument: *Provided,* That this shall only apply for CLNs that are outstanding as of the effective

date of reclassification, which shall not be on or later than 15 November 2008.

Sec. III. Applicability to Trust Institutions The guidelines shall likewise apply to trust institutions except for the following accounts:

(a) UIT Funds; and

(b) Pre-need, escrow and other accounts whose investments are regulated by or require approval from other regulatory agencies: *Provided,* That prior to the reclassification, the approval/consent and reflect the change in client's investment profile in the revised Investment Policy Statement as provided in *Appendix 83*: *Provided, further,* That in the case of managed retirement funds/ employee benefit trust accounts, such reclassification shall be aligned with the liquidity requirements resulting from the latest actuarial valuation of the fund/account.

Sec. IV. Reportorial Requirements. FIs that reclassify financial assets out of the HFT/ AFS categories shall submit a report on Reclassification of Financial Assets between Categories to the Supervisory Data Center, Supervision and Examination Sector on or before 30 November 2008.

(Circular No. 626 dated 23 October 2008 as amended by Circular No. 628 dated 31 October 2008)

ESTABLISHING THE MARKET BENCHMARKS/REFERENCE PRICES AND COMPUTATION METHOD USED TO MARK-TO-MARKET DEBT AND MARKETABLE EQUITY SECURITIES

(Appendix to Subsec. 4388Q.5 (2008 - 4391Q.3)

General Principle

As a general rule, to the extent a credible market pricing mechanism as determined by the BSP exists for a given security, that market price shall be the basis of marking-to-market. However, in the absence of a market price, a calculated price shall be used as prescribed herein.

Marking-to-Market Guidelines

To ensure consistency, the following shall be used as bases in marking-to-market debt and equity securities:

Type of Security	Market Price Basis
A. Equity Securities Listed in the Stock Exchange	
1. Traded in the Philippines	Same day closing price as quoted at the Philippine Stock Exchange. In case of halt trading/ suspension or holidays, use the last available closing price.
2. Traded Abroad	Latest available closing price from the exchange where the securities are traded.
B. Foreign Currency-Denominated Debt Securities Quoted in Major Information Systems (e.g., Bloomberg, Reuters)	
1. US Treasuries	Price as of end of day, Manila time.
2. US Agency papers such as Fannie Maes, Freddie Macs, Ginnie Maes, Municipal papers	Latest available price for the day, Manila time. In the absence of a price, use average quotes of at least three (3) regular brokers/market makers.*
3. Brady Bonds	Same as B.2.
4. For all US$-denominated government and corporate securities	Same as B.2.
5. Other foreign-currency securities	Same as B.2.

* Based on done rates if available. If done rates are not available, use the mid rate between bid and offer. If no mid rates are available, use the bid rate.

C. Foreign Currency Denominated Debt Securities Traded in a Local Registered Exchange or Market

The basis for marking-to-market foreign currency-denominated debt securities traded in a local registered exchange or market shall be the same as those used in Peso-Denominated GS in Section D below.

D. Peso-Denominated GS

The benchmark or reference prices shall be based on the weighted average of done or executed deals in a trading market registered with the SEC. In the absence of done deals, the best firm bid per benchmark tenor shall be used in calculating the benchmark: *Provided*, That the best firm offer per benchmark tenor shall likewise be included as soon as permissible under securities laws and regulations.

The benchmark or reference rate shall be computed and published in accordance with prescribed guidelines on the computation of reference rates by a Calculation Agent which is recognized by the BAP: *Provided*, That both the Calculation Agent and its method of computation are acceptable to the BSP.

To ensure the integrity of the benchmark or reference prices, the Calculation Agent shall perform the following:

1. Monitor the quality of the contributed source rates for the benchmark;

2. Monitor the data contributors and replace participants, upon consultation with the BAP, that fail to meet commitments to the benchmark;

3. Monitor the activities of the participants to ensure compliance with their commitments and for possible market manipulation and enforce sanctions on errant participants and immediately inform BAP and the BSP thereon; and

4. Review and upgrade the benchmark setting methodology upon consultation with BAP on a continuing basis, including documentation and publications thereof.

Accordingly, all data on done and firm bids/offers must be credible and verifiable and preferably sourced from trade executions and reporting systems that are part of a regulated and organized market duly licensed by the SEC where the data contributors are bound to uphold the principles of transparency, fair trading and best execution.

E. Peso-Denominated Private Debt Securities

The basis for marking-to-market peso-denominated debt securities traded in an organized market shall be the same as those used in Peso-Denominated Government Securities in Section D above.

For private debt securities which are not traded in an organized market, the marked to market value shall be based on the corresponding government security benchmark plus risk premium. The corresponding government security benchmark shall be determined according to Section D above. In determining the risk premium, the credit risk rating of the securities involved given by a BSP-recognized credit risk rating agency shall be established and taken into account whenever available. In the absence of such credit risk rating, alternative analyses may be used: *Provided*, That these are well-justified by sound risk analysis principles.

Other Guidelines

For the market valuation of securities with odd tenors, interpolated yields derived from the benchmark or reference rates in accordance with the BSP - approved guidelines for computation of reference rates in Section D above shall be used.

Penalties and Sanctions

FIs and the concerned officers found to have violated the provisions of these regulations shall be subject to the penalties prescribed under Subsec. 4388Q.5: *Provided,* That non-compliance with the above guidelines may be a basis for a finding of unsafe and unsound banking practice.

(As amended by M-2007-006 dated 28 February 2007)

GUIDELINES ON THE USE OF SCRIPLESS (RoSS) SECURITIES AS SECURITY DEPOSIT FOR THE FAITHFUL PERFORMANCE OF TRUST DUTIES

(Appendix to Sec. 4405Q and Sec. 4415Q)

Definition of Terms and Acronyms

Scripless securities and RoSS securities - refers to uncertificated securities issued by the Bureau of the Treasury (BTr) that are under the BTr's Registry of Scripless Securities

Trust institution - refers to an entity that is authorized to engage in trust business

BTr - Bureau of the Treasury

RoSS - Registry of Scripless Securities

BSP - Bangko Sentral ng Pilipinas

BSP-SES - Supervision and Examination Sector of BSP

SRSO - Supervisory Reports and Studies Office of BSP-SES

BSP-Accounting - Accounting Department of BSP

GSED - Government Securities Eligible Dealer of the BTr

DDA - refers to the regular demand deposit account of a bank/QB with BSP-Accounting

MOR - Manual of Regulations for Non-Bank Financial Institutions

Appropriate supervising and examining department or responsible supervising and examining department - refers to the Department of Thrift Banks and Non-Bank Financial Institutions

A. Basic Requirements

1. The BSP-SES shall file with BTr an application to open a RoSS Principal Securities Account where RoSS securities of trust institutions used as security deposit for trust duties shall be held. BSP-SES shall use *Annex 1* for this purpose.

2. Using *Annex 1-A*, BSP-SES shall also apply for a Client Securities Account (sub-account) for each trust institution under its RoSS Principal Securities Account to enable BSP-SES to keep track of the security deposit. BTr shall maintain Client Securities Accounts for ₱1,000 each month per account.

3. A trust institution which has a DDA with BSP-Accounting shall act as its own settlement bank.

A trust institution which does not have a DDA with the BSP-Accounting shall designate a settlement bank which will act as conduit for transferring securities for trust duties to the BSP-SES account and for paying interest, interest coupons and redemption proceeds. The trust institution shall inform the appropriate department of the SES of the designation of a settlement bank.

4. Each trust institution shall accomplish an *"Autodebit/Autocredit Authorization"* for its client securities account under the BSP-SES RoSS account. The document will authorize the BTr and the BSP to credit the DDA of the trust institution with BSP-Accounting for coupons/interest payments on securities in the BSP-SES RoSS accounts and to debit the DDA for the monthly fees payable to BTr for maintaining its client securities accounts with BSP-SES. It will also authorize

the BTR and BSP to credit the deposit account of BSP-SES with BSP-Accounting for the redemption proceeds of securities that mature while in the BSP-SES RoSS account.

A trust institution with a DDA with BSP-Accounting shall use *Annex 2-A* while a trust institution with a settlement arrangement shall use *Annex 2-B*.

5. BSP-SES shall open a deposit account with BSP-Accounting where the redemption value of securities shall be credited, in the event such securities mature while lodged in the RoSS account of BSP-SES.

6. SRSO shall be responsible for keeping track of the deposit and withdrawal of securities held under the BSP-SES Principal Securities Account and the Client Securities Accounts of the trust institutions. SRSO shall instruct BTr to transfer securities out of the BSP-SES account and the corresponding client securities accounts of trust institutions only after receiving authorization from the Director (or in his absence, the designated alternate officer) of the appropriate department of the SES.

SRSO shall also be responsible for keeping track of the BSP-SES deposit account with the BSP-Accounting representing credits for the redemption value of security deposit of trust institutions that have matured while in the RoSS account of BSP-SES. SRSO shall maintain sub-accounts for each trust institution for the purpose. SRSO shall instruct BSP-Accounting to transfer balances out of the deposit account and the corresponding sub-account of the trust institution only after receiving authorization from the Director (or in his absence, the designated alternate officer) of the appropriate department of the SES.

7. BSP-SES shall subscribe to the *Telerate* electronic trading system which is linked to BTr's RoSS and cause the installation of a *Telerate* terminal at SRSO. Trust institutions may be required to reimburse BSP-SES for whatever expenses that may be incurred in connection with the subscription.

8. Every trust institution must ensure that it has adequate security deposit for trust duties pursuant to the provisions of Subsecs. 4405Q.1, 4405Q.2, 4405Q.3 and 4405Q.4 of the MOR.

9. BTr shall provide BSP-SES with the end-of-day transaction report whenever a transaction in any client securities account is made. BTr shall also provide BSP-SES a monthly report of balances of each client securities account.

10. Every quarter, the responsible SED of BSP-SES shall determine, based on the *Report of Trust and Other Fiduciary Business and Investment Management Activities* (BSP 7-26-23) submitted by the trust institution, whether or not the trust institution's security deposit for trust duties is sufficient pursuant to the provisions of the MOR mentioned above. In case of deficiency, the department shall recommend the imposition of sanctions and/or any other appropriate action to higher authorities.

B. Procedures for Assigning RoSS Securities as Security Deposit for Trust Duties

1. The trust institution shall advise the appropriate BSP-SES department that it will transfer RoSS securities to BSP-SES. The advice should be received by the BSP-SES at least two (2) business days before the date of transfer using the prescribed form (*Annex 3*) and checking Box "b" of said form. (Box "a" shall be checked by a new trust institution that is making an initial security deposit pursuant to Subsec. 4404Q.4 of the MOR.) The advice should be sent by cc mail or by fax to be followed by an official letter duly signed by an authorized trust officer.

2. The trust institution shall electronically instruct BTr to transfer

securities from its own RoSS accounts to the BSP-SES RoSS and its corresponding Client Securities Account on the specified date. In the case of a trust institution with a settlement arrangement, the instruction shall be coursed through the settlement bank and the securities shall come from the RoSS account of the same bank.

3. BTr shall effect the transfer upon verification of RoSS balances. At the end of the day, BTr shall transmit a transaction report to SRSO containing the transfer.

4. SRSO shall provide the appropriate BSP-SES department a copy of the report.

5. The BSP-SES department concerned shall check from the report whether BTr effected the transfer indicated in the advice (*Annex 3*) sent earlier by the trust institution.

C. Procedures for Replacing RoSS Securities

1. The trust institution shall advise the appropriate deparment of the SES that it will replace existing RoSS securities assigned as security deposit. The advice should be received by the BSP-SES at least two (2) business days before the date of replacement using the prescribed form (*Annex 3*). The trust institution shall check Box "c" of the form and indicate the details of the securities to be withdrawn. The advice should be sent by cc mail or by fax to be followed by an official letter duly signed by an authorized trust officer.

2. The responsible BSP-SES department shall verify whether the securities to be replaced are in the RoSS account of BSP-SES and the sub-account of the trust institution and whether the book value of the securities to be deposited is equal to or greater than those to be withdrawn. The department concerned shall immediately communicate with the trust institution in case of a discrepancy.

3. The trust institution shall electronically instruct BTr to transfer securities from its own RoSS account to the BSP-SES RoSS accounts and its corresponding Client Securities Account on the specified date. In the case of a trust institution with a settlement arrangement, the instruction shall be coursed through the settlement bank and the securities shall come from the RoSS account of the same bank.

4. BTr shall effect the transfer upon verification of RoSS balances. At the end of the day, BTr shall transmit a transaction report to SRSO containing the transfer.

5. SRSO shall immediately provide the appropriate BSP-SES department a copy of the report.

6. The BSP-SES department concerned shall immediately check from the report whether the securities transferred to the BSP-SES account are the same securities described in the advice (*Annex 3*) sent earlier. If in order, the Director (or in his absence, the designated alternate officer) of the department concerned shall authorize SRSO to instruct BTr to transfer the securities specified to be withdrawn from the BSP-SES account to the trust institution's (or the settlement bank's) RoSS account. The Department concerned shall use *Annex 5* and check Boxes "a" and "d". Should there be any discrepancy, the department shall inform the trust institution immediately. The authority to allow the withdrawal should be transmitted to SRSO not later than the day after the replacement securities were transferred to the BSP-SES account.

The BSP-SES department concerned shall also advise the trust institution that it has approved the replacement of security deposit by using *Annex 6* and checking Boxes "a" and "d" and the appropriate box under "d" depending on whether or not the trust institution has a settlement arrangement.

7. On the same day, SRSO shall instruct BTr to transfer the securities specified to be withdrawn from the BSP-SES account to the RoSS account of the trust institution (or its settlement bank).

8. BTr shall effect the transfer/ withdrawal. At the end of the day, BTr shall send a report to SRSO containing the transfer/withdrawal.

9. SRSO shall provide the appropriate BSP-SES department a copy of the report.

10. The responsible BSP-SES department shall check from the report whether BTr effected the transfer/ withdrawal.

D. Procedures for Withdrawing RoSS Securities

1. The trust institution shall advise the appropriate BSP-SES department that it will withdraw existing RoSS securities assigned as security deposit. The advice should be received by the BSP-SES at least two (2) banking days before the date of withdrawal using the prescribed form (*Annex 4*) and indicating therein details of the securities to be withdrawn. The advice should be sent by cc mail or by fax to be followed by an official letter duly signed by an authorized trust officer.

2. The responsible BSP-SES department shall verify whether the securities to be withdrawn are in the RoSS account of BSP-SES and the Client Securities Account of the trust institution. The department shall also determine whether the amount of remaining security deposit will still be adequate in spite of the proposed withdrawal. If in order, the Director (or in his absence, the designated alternate officer) of the department concerned shall authorize SRSO to instruct BTr to transfer the securities specified to be withdrawn from the BSP-SES account to the trust institution's own RoSS account (or its settlement bank). The Department concerned shall use *Annex 5* and check Boxes "b" and "d". Should there be any discrepancy, the department shall inform the trust institution immediately. The authority to allow the withdrawal should be transmitted to SRSO not later than the date of the withdrawal indicated in the advice (*Annex 4*) sent earlier by the trust institution.

The BSP-SES department concerned shall also advise the trust institution that it has approved the withdrawal of security deposit by using *Annex 6* and checking Boxes "b" and "d" and the appropriate box under "d" depending on whether or not the trust institution has a settlement arrangement.

3. On the same date, SRSO shall instruct BTr to transfer the securities specified to be withdrawn from the BSP-SES account to the RoSS account of the trust institution (or its settlement bank).

4. BTr shall effect the transfer/ withdrawal. At the end of the day, BTr shall send to SRSO a report which contains the transfer/withdrawal.

5. SRSO shall provide the appropriate BSP-SES department a copy of the report.

6. The BSP-SES department concerned shall check from the report whether BTr effected the withdrawal stated in the advice (*Annex 4*) sent earlier by the trust institution.

E. Procedures for Crediting Interest Coupon Payments. On coupon or interest payment date, BTr shall instruct BSP-Accounting to credit the DDA of trust institutions or their designated settlement banks for coupon/interest payment of securities held under the RoSS account of BSP-SES.

F. Procedures for Crediting and Withdrawing the Redemption Value of Matured Securities that are in the BSP-SES RoSS Account

1. On maturity date, BTr shall instruct BSP-Accounting to credit the deposit account of BSP-SES with BSP-Accounting

for the redemption value of securities that mature while held as security deposit in the RoSS account of BSP-SES.

2. BTr shall send to SRSO a copy of the credit advice.

3. SRSO shall immediately provide the appropriate BSP-SES department a copy of the credit advice.

4. The responsible BSP-SES department shall immediately inform the trust institution concerned of the cash credit and shall inquire whether the trust institution intends to transfer securities to the RoSS account of the BSP-SES to replace the matured securities.

5. The trust institution shall advise the appropriate BSP-SES department that it will transfer RoSS securities to BSP-SES in place of the cash credited to the deposit account of BSP-SES with BSP-Accounting for matured securities. The trust institution shall check Box "d" of the prescribed form (*Annex 3*). The concerned department shall determine if the book value of the securities to be transferred is equal to or greater than the cash credit.

6. The trust institution shall electronically instruct BTr to transfer securities from its own RoSS accounts to the BSP-SES RoSS account and its corresponding Client Securities Account on the specified date. In the case of a trust institution with a settlement arrangement, the instruction shall be coursed through the settlement bank and the securities shall come from the RoSS account of the same bank.

7. BTr shall effect the transfer upon verification of RoSS balances. At the end of the day, BTr shall send a report to SRSO containing the transfer.

8. SRSO shall provide the appropriate BSP-SES department a copy of the report.

9. The BSP-SES department concerned shall immediately check from the report whether the securities transferred to the BSP-SES account are the same securities described in the advice (*Annex 3*) sent earlier by the trust institution. If in order, the Director (or in his absence, the designated alternate officer) of the Department shall direct the SRSO to instruct BSP-Accounting Department to debit the BSP-SES deposit account and transfer the funds to the DDA of the trust institution (or its designated settlement bank). The Department concerned shall use *Annex 5* and check Boxes "c" and "e".

The BSP-SES department concerned shall also advise the trust institution that it has approved the replacement of matured securities by using *Annex 6* and checking Boxes "c" and "e" and the appropriate box under "e" depending on whether or not the trust institution has a settlement arrangement.

10. SRSO shall direct BSP-Accounting to debit the BSP-SES deposit account and credit the same amount to the DDA of the trust institution (or its designated settlement bank) using *Annex 7*.

11. BSP-Accounting shall effect the transaction and send a copy of the debit advice to SRSO and a copy of the credit advice to the trust institution (or the designated settlement bank).

Annex 1

SUPERVISION AND EXAMINATION SECTOR

Date_____

_____
Treasurer of the Philippines
Bureau of Treasury
Palacio del Gobernador
Intramuros, Manila

Attention: Registry of Scripless Securities (RoSS)

Dear_____ :

The Supervision and Examination Sector of the Bangko Sentral ng Pilipinas (BSP-SES) hereby makes an application to open a Principal Securities Account in the Registry of Scripless Securities (RoSS) for the purpose of holding the security deposit for the faithful performance of trust duties of institutions engaged in trust business pursuant to Section 65 of R.A. No. 337, as amended.

We understand that the Bureau of the Treasury shall maintain the Principal Securities Account of BSP-SES for free.

Very truly yours,

_____
Deputy Governor

Annex 1-A

SUPERVISION AND EXAMINATION SECTOR

Date_____

_____
Treasurer of the Philippines
Bureau of Treasury
Palacio del Gobernador
Intramuros, Manila

Attention: Registry of Scripless Securities (RoSS)

Dear Ms. _____

In connection with the Principal Securities Account of BSP-SES in the Registry of Scripless Securities (RoSS), please open Client Securities Account for the following trust institutions so we can keep track of their security deposit for the faithful performance of trust duties. Please note that the settlement bank of the institution, if it is required, is also indicated.

	Name of Trust Institution	Name of Settlement Bank, where required
1.	_____	_____
2.	_____	_____
n	_____	_____

We understand that the Bureau of the Treasury will maintain the Client Securities Account for P1,000 per month per account.

Very truly yours,

_____
(Signature)
Authorized Signatory

Annex 2-A

To be used by a trust institution with own demand deposit account with BSP-Accounting

Letterhead of Trust Institution

AUTODEBIT/AUTOCREDIT AUTHORIZATION

The _____(name of trust institution)_____ hereby authorizes the Bureau of the Treasury (BTr) and the Bangko Sentral ng Pilipinas (BSP) to debit/credit our demand deposit account with BSP-Accounting for coupons/interest payment of our securities in the BSP-SES RoSS accounts; and to settle the payment of monthly maintenance fees to BTr of our client securities account under the BSP-SES RoSS account. We also authorize the BTr and the BSP to credit the Account of BSP-SES with BSP-Accounting for the redemption proceeds of our securities in the event such securities mature while in the RoSS account of BSP-SES.

This authorization will take effect on _____(indicate date)_____ .

_____
(Signature)
(Authorized Signatory)

Annex 2-B

To be used by a trust institution with settlement arrangement with a bank

Letterhead of Trust Institution

AUTODEBIT/AUTOCREDIT AUTHORIZATION

The (name of settlement bank) for the account of (name of trust institution) hereby authorizes the Bureau of the Treasury (BTr) and the Bangko Sentral ng Pilipinas (BSP) to debit/credit our demand deposit account with BSP-Accounting for coupons/interest payment of securities of the trust institution in the BSP-SES RoSS accounts; for maturing securities of the trust institution held in our RoSS Principal Securities Account with BTr; and to settle the payment of monthly maintenance fees to BTr of our client securities account under the BSP-SES RoSS account.

The (name of trust institution) also authorizes the BTr and the BSP to credit the Account of BSP-SES with BSP-Accounting for the redemption proceeds of our securities in the event such securities mature while in the RoSS account of BSP-SES.

This authorization will take effect on (indicate date) .

_____
(Signature)
(Authorized Signatory of Settlement Bank)

_____
(Signature)
(Authorized Signatory of Trust Institution)

Annex 3

Letterhead of Trust Institution

Date_____

The Director
DTBNBFI
Bangko Sentral ng Pilipinas
A. Mabini St., Manila

Dear Sir:

We are transferring on (indicate date of transfer) the following securities to your Principal Securities Account and our Client Securities Account (sub-account) as our security deposit for the faithful performance of trust duties pursuant to Section 65 of R.A. No. 337, as amended.

Type	ISIN	Purchase Date	Issue Date	Due Date	Remaining Tenor [a/]	Face Amount	Purchase Price

We are transferring the above securities:

a. ☐ As our initial deposit
b. ☐ As an additional security deposit
c. ☐ To replace the following securities which we deposited on ___(date)___.

Type	ISIN	Purchase Date	Issue Date	Due Date	Remaining Tenor [a/]	Face Amount	Purchase Price

d. ☐ To replace matured securities the redemption value of which ₱ _____ is credited to the deposit account of BSP-SES with BSP-Accounting.

Very truly yours,

_____
(Signature)
Name and Designation of Authorized Signatory

[a/] Reckoned from actual date of transfer/withdrawal

Annex 4

Letterhead of Trust Institution

Date: _____

The Director
DTBNBFI
Bangko Sentral ng Pilipinas
A. Mabini St., Manila

Dear Sir:

We wish to withdraw on (indicate date of transfer) the following securities used as security deposit for the faithful performance of trust duties from the Principal Securities Account and from our corresponding Client Securities Account (sub-account).

Type	ISIN	Purchase Date	Issue Date	Due Date	Remaining Tenor [a/]	Face Amount	Purchase Price

Very truly yours,

_____
(Signature)
Name and Designation of Authorized Signatory

[a/] Reckoned from actual date of transfer/withdrawal

Annex 5

MEMORANDUM

DTBNBFI

F o r : The Director
Supervisory Reports and Studies Office

From : The Director

Subject : Scripless Securities Used As Deposit for Trust Duties

Date :

In connection with the request of (indicate name of trust institution) dated _____ to:

a. ☐ Replace outstanding RoSS securities
b. ☐ Withdraw RoSS securities
c. ☐ Replace cash credit of matured securities with outstanding RoSS securities,

you are hereby authorized to:

d. ☐ Instruct the Bureau of Treasury to transfer the following securities out of the BSP-SES RoSS accounts to the RoSS Principal Securities Account of (indicate name of trust institution or, where applicable, the name of its settlement bank)

Type	ISIN	Purchase Date	Issue Date	Due Date	Remaining Tenor [a/]	Face Amount	Purchase Price

e. ☐ Instruct BSP-Accounting to debit the BSP-SES deposit account in the amount of ₱_____ and to transfer said amount to the demand deposit account of (indicate name of trust institution or, where applicable, the name of its designated settlement bank).

_____
(Signature)
Authorized Signatory

[a/] Reckoned from actual date of transfer/withdrawal

Annex 6

DTBNBFI

Date _____

(Name of Trust Institution) _____
(Address)

Subject : Scripless Securities Used As Deposit for Trust Duties

Dear Mr. _____:

We are pleased to inform you that we have approved your request dated _____ to:

a. ☐ Replace outstanding RoSS securities
b. ☐ Withdraw RoSS securities
c. ☐ Replace cash credit of matured securities with outstanding RoSS securities.

Accordingly, we have authorized the Supervisory Reports and Studies Office to:

d. ☐ Instruct the Bureau of Treasury to transfer the following securities out of the BSP-SES RoSS accounts to -

☐ the RoSS Principal Securities Account
☐ your settlement bank's RoSS Principal Securities Account, the securities described in your request.

e. ☐ Instruct BSP-Accounting to debit the BSP-SES deposit account in the amount of ₱_____ and to credit said amount to -

☐ your demand deposit account with BSP-Accounting
☐ your settlement bank's demand deposit account with BSP-Accounting

Very truly yours,

_____
(Signature)
Authorized Signatory

Annex 7

MEMORANDUM

DTBNBFI

For : The Director
Accounting Department

From : The Director

Date :

Subject: Security Deposit for Trust Duties

You are hereby instructed to debit our deposit account in the amount of ₱ _____ and to credit said amount to the demand deposit account of (indicate name of trust institution or, where applicable, the name of its settlement bank).

The trust institution has transferred RoSS securities to the Principal Securities Account of BSP-SES to replace the matured securities.

_____
(Signature)
Authorized Signatory

PROCEDURES ON COLLECTION OF FINES/PENALTIES FROM QUASI-BANKS AND/OR DIRECTORS/OFFICERS OF QUASI-BANKS

[Appendix to Subsecs. 4902Q.2 (2008 - 4653Q.2)]

For uniform implementation of the regulations on collection of fines/penalties from QBs and/or directors/officers of QBs, the following procedures shall be observed:

1. Upon approval of the fines/penalties by the Governor/Monetary Board, the Department/Office concerned shall send the Statement of Account (SOA)/billing letter to the QB with an advice that the penalty should be paid in full within fifteen (15) calendar days from receipt of SOA/billing letter. For entities which maintain demand deposit account (DDA) with BSP, the amount of the penalty/ies shall be automatically debited from the QB's DDA with the BSP after the lapse of the fifteen (15)-calendar day period. The QB shall likewise be advised that penalty or portion thereof which remained unpaid after the lapse of said fifteen (15)-day period shall be subject to additional charge of six percent (6%) per annum reckoned from the business day immediately following the end of the fifteen (15)-day period up to the day of actual payment.

2. On the business day immediately following the end of said fifteen (15)-day period, unpaid penalties shall be automatically debited, without additional charge, against the QB's DDA with the BSP by the Comptrollership Sub-sector (CoSS) based on the amount booked by the Department/Office concerned after first confirming with the CoSS the sufficiency of the QB's DDA balance to cover the amount of the penalty.

3. If, based on its confirmation with the CoSS, the Department/Office concerned received information that the QB's DDA balance is insufficient to cover the amount of the penalty, it shall accordingly advise and request the bank to immediately fund its DDA.

4. As soon as it is funded, the QB's DDA shall be debited by the CoSS for the amount of the penalty, plus the six percent (6%) additional charge for late payment of the penalty reckoned from the business day immediately following the end of the fifteen (15)-day period up to the day of actual payment, based on the amount booked by the Department/Office concerned.

5. Payment by QBs of penalty, plus the additional charge if any by check or demand draft shall be made directly to the BSP Cash Department or to BSP Regional Cash Units in accordance with the provisions of Subsec. 4902Q.4.

6. In the case of penalty/ies imposed on QB directors/officers, said directors/officers shall be advised by the Department/Office concerned to pay within fifteen (15) calendar days from receipt of the SOA/billing letter directly to the BSP in the form of cash or check and in accordance with the provisions of Subsec. 4902Q.4. Penalty or portion thereof which remained unpaid after the lapse of said fifteen (15)-day period shall also be subject to additional charge of six percent (6%) per annum reckoned from the banking day immediately following the end of the fifteen (15)-day period up to the day of actual payment.

(As amended by Circular No. 662 dated 09 September 2009)

PROFORMA PAYMENT FORM

[Appendix to Subsec. 4902Q.2 (2008 - 4653Q.2)]

BANGKO SENTRAL NG PILIPINAS
Manila

_____
(Name of Department/Office)

FOR -

The Director
Cash Department

Please issue OFFICIAL RECEIPT to _____(name of payor)_____ as payment of

_____(nature of payment)_____ and effect the following accounting entries:

Account Code	Account Title/Description Accountee Type/Code/Name	DR/CR	Amount
			P

Total Debit _____
Total Credit P_____

Approved by: _____
(Name of BSP Official/Position)

Date:_____

Received by:_____
Date:

Official Receipt No:_____
Date:

(As amended by Circular No. 662 dated 09 September 2009)

(RESERVED)

CERTIFICATION OF COMPLIANCE WITH ANTI-MONEY LAUNDERING REGULATIONS

C E R T I F I C A T I O N

Pursuant to the provisions of Section 2 of BSP Circular No. 279 dated 02 April 2001, we hereby certify:

1. That we have monitored (Name of quasi-bank)'s compliance with R.A. No. 9160 (Anti-Money Laundering Act of 2001) as well as with BSP Circular Nos. 251, 253, 259 and 302;

2. That the quasi-bank is complying with the required customer identification, documentation of all new clients, and continued monitoring of customer's activities;

3. That the quasi-bank is also complying with the requirement to record all transactions and to maintain such records including the record of customer identification for at least five (5) years;

4. That the quasi-bank does not maintain anonymous or fictitious accounts; and

5. That we conduct regular anti-money laundering training sessions for all quasi-bank officers and selected staff members holding sensitive positions.

_____ _____
(Name of President or officer of equivalent rank) (Name of Compliance Officer)

SUBSCRIBED AND SWORN to before me, _____ this ____ day of _____, affiant/s exhibiting to me their Community Tax Certificate No.(s) as follows:

Name	Community Tax Cert. No	Date/Place Issued

_____
Notary Public

Doc. No. _____;
Page No. _____;
Book No. _____;
Series of 20___

Anti-Money Laundering Council No. 292

RULES ON SUBMISSION OF COVERED TRANSACTION REPORTS AND SUSPICIOUS TRANSACTION REPORTS BY COVERED INSTITUTIONS[1]

1. All covered institutions are required to file Suspicious Transaction Reports (STRs) on transactions involving all kinds of monetary instruments or property.

2. Banks shall file covered transaction reports (CTRs) on transactions involving all kinds of monetary instruments or property, i.e., in cash or non-cash, whether in domestic or foreign currency.

3. Covered institutions, other than banks, shall file CTRs on transactions in cash or foreign currency or other monetary instruments (other than checks) or properties. Due to the nature of the transactions in the stock exchange, only the brokers-dealers shall be required to file CTRs and STRs. The PSE, PCD, SCCP and transfer agents are exempt from filing CTRs. They, are however, required to file STRs when the transactions that pass through them are deemed to be suspicious.

4. Where the covered institution engages in bulk transactions with a bank, i.e., deposits of premium payments in bulk or settlements of trade, and the bulk transactions do not distinguish clients and their respective transaction amounts, said covered institutions shall be required to file CTRs on its clients whose transactions exceed ₱500,000 and are included in the bulk transactions.

5. With respect to insurance companies, when the total amount of the premiums for the entire year, regardless of the mode of payment (monthly, quarterly, semi-annually or annually), exceeds ₱500,000, such amount shall be reported as a covered transaction, even if the amounts of the amortizations are less than the threshold amount. The CTR shall be filed upon payment of the first premium amount, regardless of the mode of payment. Under this rule, the insurance company shall file the CTR only once every year until the policy matures or rescinded, whichever comes first.

6. The submission of CTRs is deferred until the AMLC directs otherwise. Submission of STRs, however, are not deferred and covered institutions are mandated to submit such STRs when the circumstances so require.

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[1] a. The Anti-Money Laundering Council (AMLC), in the exercise of its authority under Sections 7(1) and 9 of Republic Act No. 9160, otherwise known as the "Anti-Money Laundering Act of 2001", as amended, and its Revised Implementing Rules and Regulations, resolved to:

(1) Defer reporting by covered institutions to AMLC of the following "non-cash, no/low risk covered transactions:

- Transactions between banks and the BSP;
- Transactions between banks operating in the Philippines;
- Internal operating expenses of the banks;
- Transactions involving transfer of funds from one deposit account to another deposit account of the same person within the same bank;
- Roll-overs of placements of time deposits; and
- Loan interest/principal payment debited against borrower's deposit account maintained with the lending bank.

(2) Request the BSP-supervised institutions, through the Association of Bank Compliance Officers (ABCOMP), to determine and report to AMLC the specific transactions falling within the purview of the aforesaid BSP-identified categories on "non-cash, no/low risk" covered transactions.

b. All covered institutions should:

(1) Submit corresponding electronic copy versions, in the required format, of those STRs previously submitted in hard copy or the hard copy version of those submitted only in electronic form, as the case may be, retroactive to 05 January 2004; and

(2) Re-submit in required electronic form, those CTRs that have been submitted previously in hard copy or in diskette not in the required format, retroactive to 23 March 2003.

(As amended by CL-2009-037 dated 04 May 2009)

CUSTOMER DUE DILIGENCE FOR BANKS AND QUASI-BANKS

1. Customer acceptance policy

QBs should develop clear customer acceptance policies and procedures, including a description of the types of customer that are unacceptable to QB management. In preparing such policies, factors such as customers' background, country of origin, public or high profile position, business activities or other risk indicators should be considered. QBs should develop graduated customer acceptance policies and procedures that require more extensive due diligence for high risk customers. For example, the policies may require the most basic account-opening requirements for a working individual with a small account balance, whereas quite extensive due diligence may be deemed essential for an individual with a high net worth whose source of funds is unclear. Decisions to enter into business relationships with high risk customers, *such as individuals holding important/prominent positions, public or private* (see below), should be taken exclusively at senior management level.

2. Customer identification

Customer identification is an essential element of KYC standards. A customer is defined as any person or entity that keeps an account with a quasi-bank and any person or entity on whose behalf an account is maintained, as well as the beneficiaries of transactions conducted by professional financial intermediaries. Specifically, a customer should include an account-holder and the beneficial owner of an account. A customer should also include the beneficiary of a trust, an investment fund, a pension fund or a company whose assets are managed by an asset manager, or the grantor of a trust.

QBs should establish a systematic procedure for verifying the identity of new customers and should never enter a business relationship until the identity of a new customer is satisfactorily established. QBs should "document and enforce policies for identification of customers and those acting on their behalf"[1]. The best documents for verifying the identity of customers are those most difficult to obtain illicitly and to counterfeit, *such as passport, driver's license or alien certificate of registration*. Special attention should be exercised in the case of non-resident customers and in no case should a QB short-circuit identity procedures just because the new customer is unable to present himself for interview. The QB should always ask itself why the customer has chosen to open an account in a foreign jurisdiction.

The customer identification process applies naturally at the outset of the relationship, but there is also a need to apply KYC standards to existing customer accounts. Where such standards have been introduced only recently and do not as yet apply fully to existing customers, a risk assessment exercise can be undertaken and priority given to obtaining necessary information, where it is deficient, in respect of the higher risk cases. An appropriate time to review the information available on existing customers is when a transaction of significance takes place, or when there is a material change in the way that the account is operated. However, if a QB is aware that it lacks sufficient information about an existing high-risk customer, it should take steps to

[1] Core Principles Methodology, Essential Criterion 2.

ensure that all relevant information is obtained as quickly as possible. In addition, the supervisor needs to set an appropriate target date for completion of a KYC review and regularization of all existing accounts. In any event, a QB should undertake regular reviews of its customer base to establish that it has up-to-date information and a proper understanding of its account holders' identity and of their business.

QBs that offer private banking services are particularly exposed to reputational risk. Private quasi-banking by nature involves a large measure of confidentiality. Private quasi-banking accounts can be opened in the name of an individual, a commercial business, a trust, an intermediary or a personalized investment company. In each case reputational risk may arise if the QB does not diligently follow established KYC procedures. In no circumstances should private quasi-banking operations function autonomously, or as a "QB within a QB"[1], and no part of the QB should ever escape the required procedures. This means that all new clients and new accounts should be approved by at least one person other than the private quasi-banking relationship manager. If particular safeguards are put in place internally to protect confidentiality of private quasi-banking customers and their business, QBs must still ensure that at least equivalent scrutiny and monitoring of these customers and their business can be conducted, e.g., they must be open to review by compliance officers and auditors.

2.1 General identification requirements

QBs need to obtain all information necessary to establish to their full satisfaction the identity of each new customer and the purpose and intended nature of the business relationship. The extent and nature of the information depends on the type of applicant (personal, corporate, etc.) and the expected size of the account. National supervisors are encouraged to provide guidance to assist QBs in their designing their own identification procedures. Examples of the type of information that would be appropriate are set out in Annex Q-23-c-1.

QBs should apply their full KYC procedures to applicants that plan to transfer an opening balance from another FI, bearing in mind that the previous account manager may have asked for the account to be removed because of a concern about dubious activities.

QBs should never agree to open an account or conduct ongoing business with a customer who insists on anonymity or "bearer" status or who gives a fictitious name. Nor should confidential numbered[2] accounts function as anonymous accounts but they should be subject to exactly the same KYC procedures as all other customer accounts, even if the test is carried out by selected staff. Whereas a numbered account can offer additional protection for the identity of the account-holder, the identity must be known to a sufficient number of staff to operate proper due diligence. Such accounts should in no circumstances be used to hide the customer identity from a QB's compliance function or from the supervisors.

QBs need to be vigilant in preventing corporate business entities from being used by natural persons as a method of operating anonymous accounts. Personal asset holding vehicles, such as international business companies (IBCs), may make proper identification of customers or beneficial owners difficult. A QB should take all steps necessary to satisfy itself that it knows the true identity of the ultimate owner of all such entities.

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[1] Some QBs insulate their private quasi-banking functions or create Chinese walls as a means of providing additional protection for customer confidentiality.

[2] In a numbered account, the name of the beneficial owner is known to the QB but is substituted by an account number or code name in subsequent documentation.

2.2 Specific identification issues

There are a number of more detailed issues relating to customer identification which need to be addressed. Particular comments are invited on the issues mentioned in this section. Several of these are currently under consideration by the FATF as part of a general review of its forty recommendations, and the Working Group recognizes the need to be consistent with the FATF.

2.2.1 Trust, nominee and fiduciary accounts or client accounts opened by professional intermediaries

Trust, nominee and fiduciary accounts can be used to avoid customer identification procedures. While it may be legitimate under certain circumstances to provide an extra layer of security to protect the confidentiality of legitimate private quasi-banking customers, it is essential that the true relationship is understood. QBs should establish whether the customer is acting on behalf of another person as trustee, nominee or professional intermediary (e.g. a lawyer or an accountant). If so, a necessary precondition is receipt of satisfactory evidence of the identity of any intermediaries and of the persons upon whose behalf they are acting, as well as details of the nature of the trust or other arrangements in place.

QBs may hold "pooled' accounts (e.g. client accounts managed by law firms) or accounts opened on behalf of pooled entities, such as mutual funds and money managers. In such cases, QBs have to decide, given the circumstances, whether the customer is the intermediary, or whether it would be more appropriate to look through the intermediary to the ultimate beneficial owners. In each case, the identity of the customer that is subject to due diligence should be clearly established. The beneficial owners should be verified where possible. Where not, the QBs should perform due diligence on the intermediary and establish to its complete satisfaction that the intermediary has a sound due diligence process for each of its clients.

Special care needs to be exercised in initiating business transactions with companies that have nominee shareholders or shares in bearer form. Satisfactory evidence of the identity of beneficial owners of all companies needs to be obtained.

The above procedures may prove difficult for QBs in some countries to follow. In the case of professional intermediaries such as lawyers, there might exist professional codes of conduct preventing the dissemination of information concerning their clients. The FATF is currently engaged in a review of KYC procedures governing accounts opened by lawyers on behalf of clients. The Working Group has therefore not taken a definitive position on this issue.

2.2.2 Introduced business

The performance of identification procedures can be time consuming and there is a natural desire to limit any inconvenience for new customers. In some countries, it has therefore become customary for QBs to rely on the procedures undertaken by other QBs or introducers when business is being referred. In doing so, QBs risk placing excessive reliance on the due diligence procedures that they expect the introducers to have performed. Relying on due diligence conducted by an introducer, however reputable, does not in any way remove the ultimate responsibility of the recipient QB to know its customers and their business. In particular, QBs should not rely on introducers that are subject to weaker standards than those governing the QBs' own KYC procedures or that are unwilling to share copies of due diligence documentation.

The FATF is currently engaged in a review of the appropriateness of eligible introducers, i.e. whether they should be confined to reputable QBs only or should extend to other regulated institutions, whether a QB should establish a contractual relationship with its introducers and whether it is appropriate to rely on a third party introducer at all. The Working Group is still developing its thinking on this topic.

2.2.3 Reputational risk

Business relationship with individuals holding important/*prominent positions, public or private,* and with persons or companies clearly related to them may expose a QB to significant reputational and/or legal risks.

Accepting and managing funds from such persons could put at risk the QB's own reputation and can undermine public confidence in the ethical standards of an entire financial centre, since such cases usually receive extensive media attention and strong political reaction, even if the illegal origin of the assets is often difficult to prove. In addition, the QB may be subject to costly information requests and seizure orders from law enforcement or judicial authorities (including international mutual assistance procedures in criminal matters) and could be liable to actions for damages by the state concerned or the victims of a regime. Under certain circumstances, the QB and/or its officers and employees themselves can be exposed to charges of money laundering, if they know or should have known that the funds stemmed from corruption or other serious crimes.

3. On-going monitoring of high risk accounts

On-going monitoring of accounts and transactions is an essential aspect of effective KYC procedures. QBs can only effectively control and reduce their risk if they have an understanding of normal and reasonable account activity of their customers. Without such knowledge, they are likely to fail in their duty to report suspicious transactions to the appropriate authorities in cases where they are required to do so. The on-going monitoring process includes the following:

QBs should develop "clear standards on what records must be kept on customer identification and individual transactions and the retention period".[1] As the starting point and natural follow-up of the identification process, QBs should obtain and keep up to date customer identification papers and retain them for at least five years after an account is closed. They should also retain all financial transaction records for at least five years after the transaction has taken place.

QBs should ensure that they have adequate management information systems to provide managers and compliance officers with timely information needed to identify, analyse and effectively monitor higher risk customer accounts. The types of reports that may be needed include reports of missing account opening documentation, transactions made through a customer account that are unusual, and aggregations of a customer's total relationship with the QB.

Senior management of a QB in charge of private quasi-banking business should know the personal circumstances of the QB's large/important customers and be alert to sources of third party information. Every QB should draw its own distinction between large/important customers and others, and set threshold indicators for them accordingly, taking into account the country of origin and other risk factors. Significant transactions

[1] Core Principles Methodology, Essential Criterion 2

by high-risk customers should be approved by a senior manager.

QBs should have systems in place to detect unusual or suspicious patterns of activity. This can be done by establishing limits for a particular class or category of accounts. Particular attention should be paid to transactions that exceed these limits. Certain types of transactions should alert QBs to the possibility that the customer is conducting undesirable activities. They may include transactions that do not make economic or commercial sense, or that involve large amounts of cash deposits that are not consistent with the normal and expected transactions of the customer. Very high account turnover, inconsistent with the size of the balance, may indicate that funds are being "washed" through the account. A list of suspicious activities drawn up by supervisors can be very helpful to QBs.

QB should develop a clear policy and internal guidelines, procedures and controls and remain especially vigilant regarding business relationships with *individuals holding important/prominent positions, public or private,* and high profile individuals or with persons and companies that are clearly related to or associated with them[1].

4. Risk Management

Effective KYC procedures embrace routines for proper management oversight, systems and controls, segregation of duties, training and other related policies. The board of directors of the QB should be fully committed to an effective KYC programme by establishing appropriate procedures and ensuring their effectiveness. QBs should appoint a senior officer with explicit responsibility for ensuring that the QB's policies and procedures are, at a minimum, in accordance with local supervisory practice. QBs should have clear written procedures, communicated to all personnel, for staff to report suspicious transactions to a specified senior manager. That manager must then assess whether the QB's statutory obligations under recognized suspicious activity reporting regimes require the transaction to be reported to the appropriate law enforcement and supervisory authorities.

All QBs must have an ongoing employee-training programme so that QB staff is adequately trained in KYC procedures. The timing and content of training for various sectors of staff will need to be adapted by the QB for its own needs. Training requirements should have a different focus for new staff, front-line staff, compliance staff or staff dealing with new customers. New staff should be educated in the importance of KYC policies and the basic requirements at the QB. Front-line staff members who deal directly with the public should be trained to verify the customer identity for new customers, to exercise due diligence in handling accounts of existing customers on an ongoing basis and to detect patterns of suspicious activity. Regular refresher training should be provided to ensure that staff is reminded of their responsibilities and is kept informed of new developments. It is crucial that all relevant staff fully understand the need for and implement KYC policies consistently. A culture within QBs that promotes such understanding is the key to successful implementation.

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[1] It is unrealistic to expect the QB to know or investigate every distant family, political or business connection of a foreign customer. The need to pursue suspicions will depend on the size of the assets or turnover, pattern of transactions, economic background, reputation of the country, plausibility of the customer's explanations etc. It should however be noted that *individuals holding important/prominent positions, public or private* (or rather their family members and friends) would not necessarily present themselves in that capacity, but rather as ordinary (albeit wealthy) business people, masking the fact they owe their high position in a legitimate business corporation only to their privileged relation with the holder of the public office.

APP. Q-23-c
08.12.31

QBs' internal audit and compliance functions have important responsibilities in evaluating and ensuring adherence to KYC policies and procedures. As a general rule, the compliance function provides an independent evaluation of the QB's own policies and procedures, including legal and regulatory requirements. Its responsibilities should include ongoing monitoring of staff performance through sample testing of compliance and review of exception reports to alert senior management or the Board of Directors if it believes management is failing to address KYC procedures in a responsible manner.

Internal audit plays an important role in independently evaluating the risk management and controls, discharging its responsibility to the Audit Committee of the Board of Directors or a similar oversight body through periodic evaluations of the effectiveness of compliance with KYC policies and procedures. Management should ensure that audit functions are staffed adequately with individuals who are well-versed in such policies and procedures. In addition, internal auditors should be proactive in following-up their findings and criticisms.

GENERAL IDENTIFICATION REQUIREMENTS

This annex presents a suggested list of identification requirements for personal customers and corporates. National supervisors are encouraged to provide guidance to assist QBs in designing their own identification procedures.

Personal customers

For personal customers, QBs need to obtain the following information:

Name and/or names used,

permanent residential address,

date and place of birth,

name of employer or nature of self-employment/business,

specimen signature, and

source of funds.

Additional information would relate to nationality or country of origin, public or high profile position, etc. QBs should verify the information against original documents of identity issued by an official authority (examples including identity cards and passports). Such documents should be those that are most difficult to obtain illicitly. In countries where new customers do not possess the prime identity documents, e.g., identity cards, passports or driving licenses, some flexibility may be required. However, particular care should be taken in accepting documents that are easily forged or which can be easily obtained in false identities. Where there is face to face contact, the appearance should be verified against an official document bearing a photograph. Any subsequent changes to the above information should also be recorded and verified.

Corporate and other business customers

For corporate and other business customers, QBs should obtain evidence of their legal status, such as an incorporation document, partnership agreement, association documents or a business licence. For large corporate accounts, a financial statement of the business or a description of the customer's principal line of business should also be obtained. In addition, if significant changes to the company structure or ownership occur subsequently, further checks should be made. In all cases, QBs need to verify that the corporation or business entity exists and engages in its stated business. The original documents or certified copies of certificates should be produced for verification.

GENERAL GUIDE TO ACCOUNT OPENING AND CUSTOMER IDENTIFICATION

1. The Basel Committee on Banking Supervision in its paper on *Customer Due Diligence for Banks* published in October 2001 referred to the intention of the Working Group on Cross-border Banking[1] to develop guidance on customer identification. Customer identification is an essential element of an effective customer due diligence programme which banks need to put in place to guard against reputational, operational, legal and concentration risks. It is also necessary in order to comply with anti-money laundering legal requirements and a prerequisite for the identification of bank accounts related to terrorism.

2. What follows is account opening and customer identification guidelines and a general guide to good practice based on the principles of the Basel Committee's *Customer due diligence for banks* paper. This document, which has been developed by the Working Group on Cross-border Banking, does not cover every eventuality, but instead focuses on some of the mechanisms that banks can use in developing an effective customer identification programme.

3. These guidelines represent a starting point for supervisors and banks in the area of customer identification. This document does not address the other elements of the *Customer Due Diligence for banks* paper, such as the ongoing monitoring of accounts. However, these elements should be considered in the development of effective customer due diligence, anti-money laundering and combating the financing of terrorism procedures.

4. These guidelines may be adapted for use by national supervisors who are seeking to develop or enhance customer identification programmes. However, supervisors should recognize that any customer identification programme should reflect the different types of customers (individual vs. institution) and the different levels of risk resulting from a customer's relationship with a bank. Higher risk transactions and relationships, such as those with politically exposed persons or organizations, will clearly require greater scrutiny than lower risk transactions and accounts.

5. Guidelines and best practices created by national supervisors should also reflect the various types of transactions that are most prevalent in the national banking system. For example, non-face-to-face opening of accounts may be more prevalent in one country than another. For this reason the customer identification procedures may differ between countries.

6. Some identification documents are more vulnerable to fraud than others. For those that are most susceptible to fraud, or where there is uncertainty concerning the validity of the document(s) presented, the bank should verify the information provided by the customer through additional inquiries or other sources of information.

7. Customer identification documents should be retained for at least five years after an account is closed. All financial transaction records should be retained for at least five years after the transaction has taken place.

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[1] The Working Group on Cross-border Banking is a joint group consisting of members of the Basel Committee and of the Offshore Group of Banking Supervisors.

8. These guidelines are divided into two sections covering different aspects of customer identification. Section A describes what types of information should be collected and verified for natural persons seeking to open accounts or perform transactions. Section B describes what types of information should be collected and verified for institutions and is in two parts, the first relating to corporate vehicles and the second to other types of institutions.

9. All the terms used in these guidelines have the same meaning as in the *Customer due diligence for banks* paper.

A. Natural Persons

10. For natural persons the following information should be obtained, where applicable:

- legal name and any other names used (such as maiden name);
- correct permanent address (the full address should be obtained; a Post Office box number is not sufficient);
- telephone number, fax number, and e-mail address;
- date and place of birth;
- nationality;
- occupation, public position held and/or name of employer;
- an official person identification number or other unique identifier contained in an unexpired official document (e.g. passport, identification card, residence permit, social security records, driving license) that bears a photograph of the customer;
- type of account and nature of the banking relationship;
- signature.

11. The bank should verify this information by at least one of the following methods:

- confirming the date of birth from an official document (e.g. birth certificate, passport, identity card,social security records);
- confirming the permanent address (e.g. utility bill, tax assessment, bank statement, a letter from a public authority);
- contacting the customer by telephone, by letter or by e-mail to confirm the information supplied after an account has been opened (e.g. a disconnected phone, returned mail, or incorrect e-mail address should warrant further investigation);
- confirming the validity of the official documentation provided through certification by an authorized person (e.g. embassy official, notary public).

12. The examples quoted above are not the only possibilities. In particular jurisdictions there may be other documents of an equivalent nature which may be produced as satisfactory evidence of customer's identity.

13. FIs should apply equally effective customer identification procedures for non-face-to-face customers as for those available for interview.

14. From the information provided in paragraph 10, FIs should be able to make an initial assessment of a customer's risk profile. Particular attention needs to be focused on those customers identified thereby as having a higher risk profile and additional inquiries made or information obtained in respect of those customers to include the following:

- evidence of an individual's permanent address sought through a credit reference agency search, or through independent verification by home visits;
- personal reference (i.e., by an existing customer of the same institution);
- prior bank reference and contact with the bank regarding the customer;
- source of wealth;
- verification of employment, public position held (where appropriate).

15. For one-off or occasional transactions where the amount of the transaction or series of linked transactions does not exceed an established minimum

monetary value, it might be sufficient to require and record only name and address.

16. It is important that the customer acceptance policy is not so restrictive that it results in a denial of access by the general public to banking services, especially for people who are financially or socially disadvantaged.

B. Institutions

17. The underlying principles of customer identification for natural persons have equal application to customer identification for all institutions. Where in the following the identification and verification of natural persons is involved, the foregoing guidance in respect of such persons should have equal application.

18. The term institution includes any entity that is not a natural person. In considering the customer identification guidance for the different types of institutions, particular attention should be given to the different levels of risk involved.

I. Corporate Entities

19. For corporate entities (i.e. corporations and partnerships), the following information should be obtained:

- name of institution;
- principal place of institution's business operations;
- mailing address of institution;
- contact telephone and fax numbers;
- some form of official identification number, if available (e.g. tax identification number);
- the original or certified copy of the Certificate of Incorporation and Memorandum and Articles of Association;
- the resolution of the Board of Directors to open an account and identification of those who have authority to operate the account;
- nature and purpose of business and its legitimacy.

20. The bank should verify this information by at least one of the following methods:

- for established corporate entities – reviewing a copy of the latest report and accounts (audited, if available);
- conducting an inquiry by a business information service, or an undertaking from a reputable and known firm of lawyers or accountants confirming the documents submitted;
- undertaking a company search and/or other commercial enquiries to see that the institution has not been, or is not in the process of being, dissolved, struck off, wound up or terminated;
- utilising an independent information verification process, such as by accessing public and private databases;
- obtaining prior bank references;
- visiting the corporate entity, where practical;
- contacting the corporate entity by telephone, mail or e-mail.

21. The bank should also take reasonable steps to verify the identity and reputation of any agent that opens an account on behalf of a corporate customer, if that agent is not an officer of the corporate customer.

Corporations/Partnerships

22. For corporations/partnerships, the principal guidance is to look behind the institution to identify those who have control over the business and the company's/partnership's assets, including those who have ultimate control. For corporations, particular attention should be paid to shareholders, signatories, or others who inject a significant proportion of the capital or financial support or otherwise exercise control. Where the owner is another corporate entity or trust, the objective is to undertake reasonable measures to look behind that company or entity and to verify the identity of the

principals. What constitutes control for this purpose will depend on the nature of a company, and may rest in those who are mandated to manage funds, accounts or investments without requiring further authorization, and who would be in a position to override internal procedures and control mechanisms. For partnerships, each partner should be identified and it is also important to identify immediate family members that have ownership control.

23. Where a company is listed on a recognized stock exchange or is a subsidiary of such a company then the company itself may be considered to be the principal to be identified. However, consideration should be given to whether there is effective control of a listed company by an individual, small group of individuals or another corporate entity or trust. If this is the case then those controllers should also be considered to be principals and identified accordingly.

II. Other Types of Institution

24. For the account categories referred to paragraphs 26 to 34, the following information should be obtained in addition to that required to verify the identity of the principals:

- name of account;
- mailing address;
- contact telephone and fax numbers;
- some form of official identification number, if available (e.g. tax identification number);
- description of the purpose/activities of the account holder (e.g. in a formal constitution);
- copy of documentation confirming the legal existence of the account holder (e.g. register of charities).

25. The bank should verify this information by at least one of the following:

- obtaining an independent undertaking from a reputable and known firm of lawyers or accountants confirming the documents submitted;
- obtaining prior bank references;
- accessing public and private databases or official sources.

Retirement Benefit Programmes

26. Where an occupational pension programme, employee benefit trust or share option plan is an applicant for an account the trustee and any other person who has control over the relationship (e.g. administrator, programme manager, and account signatories) should be considered as principals and the bank should take steps to verify their identities.

Mutuals/Friendly Societies, Cooperatives and Provident Societies

27. Where these entities are an applicant for an account, the principals to be identified should be considered to be those persons exercising control or significant influence over the organization's assets. This will often include board members plus executives and account signatories.

Charities, Clubs and Associations

28. In the case of accounts to be opened for charities, clubs, and societies, the bank should take reasonable steps to identify and verify at least two signatories along with the institution itself. The principals who should be identified should be considered to be those persons exercising control or significant influence over the organization's assets. This will often include members of a governing body or committee, the President, any board members, the treasurer, and all signatories.

29. In all cases independent verification should be obtained that the persons involved are true representatives of the institution. Independent confirmation should also be obtained of the purpose of the institution.

Trusts and Foundations

30. When opening an account for a trust, the bank should take reasonable steps to verify the trustee(s), the settler(s) of the trust (including any persons settling assets into the trust) any protector(s), beneficiary(ies), and signatories. Beneficiaries should be identified when they are defined. In the case of a foundation, steps should be taken to verify the founder, the managers/directors and the beneficiaries.

Professional Intermediaries

31. When a professional intermediary opens a client account on behalf of a single client that client must be identified. Professional intermediaries will often open "pooled" accounts on behalf of a number of entities. Where funds held by the intermediary are not co-mingled but where there are "sub-accounts" which can be attributable to each beneficial owner, all beneficial owners of the account held by the intermediary should be identified. Where the funds are co-mingled, the bank should look through to the beneficial owners; however, there may be circumstances which should be set out in supervisory guidance where the bank may not need to look beyond the intermediary (e.g. when the intermediary is subject to the same due diligence standards in respect of its client base as the bank).

32. Where such circumstances apply and an account is opened for an open or closed ended investment company, unit trust or limited partnership which is also subject to the same diligence standards in respect of its client base as the bank, the following should be considered as principals and the bank should take steps to identify:

- the fund itself;
- its directors or any controlling board where it is a company;
- its trustee where it is a unit trust;
- its managing (general) partner where it is a limited partnership;
- account signatories;
- any other person who has control over the relationship e.g. fund administrator or manager.

33. Where other investment vehicles are involved, the same steps should be taken as in paragraph 32 where it is appropriate to do so. In addition all reasonable steps should be taken to verify the identity of the beneficial owners of the funds and of those who have control of the funds.

34. Intermediaries should be treated as individual customers of the bank and the standing of the intermediary should be separately verified by obtaining the appropriate information drawn from the itemised lists included in paragraphs 19-20 above.

Anti-Money Laundering Council Resolution No. 02
Series of 2005

Pursuant to Section 9-c of the Anti-Money Laundering Act, as amended, covered institutions (CIs) shall report to the AMLC all covered transactions and suspicious transactions within five (5) working days from occurrence thereof, subject to the circumstances described in Resolution No. 292 dated 24 October 2003 which remains in full force and effect.

WHEREFORE, the Council, resolves as it hereby resolved, to approve the following policies and guidelines in reckoning CIs' compliance with the prescribed reporting period:

1. The following non-working days are excluded from the counting of the prescribed reporting period:

- weekend (Saturday and Sunday)
- official regular national holiday
- officially declared national holiday (special non-working day nationwide)
- officially declared local holiday in the locality where AMLC Secretariat Office is located

2. A "non-reporting day" may be declared by the AMLC Secretariat when the File Transfer and Reporting Facility (FTRF), used by the CIs in transmitting their electronic reports to AMLC, is unavailable to all CIs for at least five (5) consecutive hours during the day

- AMLC-declared "non-reporting day" is excluded from the counting of the prescribed reporting period.
- The Executive Director of the AMLC Secretariat (or the Officer-in-charge) is authorized to declare such day as a "non-reporting" day upon notification and justification by the Deputy Director of IMAS AMLC Secretariat.

3. Local holidays, except for officially declared local holidays in the locality where the AMLC Secretariat Office is located, are treated as working days even for CIs located in such locality declared as on holiday, and hence, included in the counting of the prescribed reporting period. However, the CIs affected may file a deviation request with the AMLC Secretariat.

- CI's request for deviation shall be subject to approval of the Executive Director of the AMLC Secretariat (or the Officer-in-charge) upon recommendation of the Deputy Director of IMAS AMLC Secretariat. It shall be the basis of manually recomputing whatever penalties that would be automatically computed by TMAS.

4. Officially-declared non-working days in localities or regions affected by natural calamities such as flood, typhoon, earthquake, etc. may be excluded from the counting of the prescribed reporting period for CIs located in affected localities or regions subject to submission of deviation request by the CI.

- CI's request for deviation shall be subject to approval of the Executive Director of the AMLC Secretariat (or the Officer-in-charge) upon recommendation of the Deputy Director of IMAS AMLC Secretariat. It shall be the basis of manually recomputing whatever penalties that would be automatically computed by TMAS.

WHEREFORE, the Council, resolves as it hereby resolved, to consider and include the foregoing policies and guidelines in the ongoing development and implementation of AMLC's Transaction Monitoring and Analysis System (TMAS) and specifically, for the computation of the penalty for delayed reporting by the CIs.

ACTIVITIES WHICH MAY BE CONSIDERED UNSAFE AND UNSOUND PRACTICES

(Appendix to Secs. 4149Q and 4408Q and Subsec. 4301Q.6)

The following activities are considered only as guidelines and are not irrebutably presumed to be unsafe or unsound. Conversely, not all practices which might under the circumstances be termed unsafe or unsound are mentioned here. The Monetary Board may now and then consider other acts/omissions as unsafe or unsound practices.

a. Operating with management whose policies and practices are detrimental to the QB/trust entity and jeopardize the safety of its deposit substitutes/trust accounts.

b. Operating with total adjusted capital and reserves that are inadequate in relation to the kind and quality of the assets of the QB/trust entity.

c. Operating in a way that produces a deficit in net operating income without adequate measures to ensure a surplus in net operating income in the future.

d. Operating with a serious lack of liquidity, especially in view of the asset and deposit substitute/liability structure of the QB/trust entity.

e. Engaging in speculative and hazardous investment policies.

f. Paying excessive cash dividends in relation to the capital position, earnings capacity and asset quality of the QB/trust entity.

g. Excessive reliance on large, high-cost or volatile borrowings to fund aggressive growth that may be unsustainable.

For this purpose, a QB is considered offering high-cost borrowings if the effective interest rate paid on said borrowings and/or non-cash incentives is fifty percent (50%) over the prevailing comparable market median rate for similar QB categories, maturities and currency denomination.

h. Excessive reliance on letters of credit either issued by the QB/trust entity or accepted as collateral to loans advanced.

i. Excessive amounts of loan participations sold.

j. Paying interest on participations without advising participating institution that the source of interest was not from the borrower.

k. Selling participations without disclosing to the purchasers of those participations material, non-public information known to the QB/trust entity.

l. Failure to limit, control and document contingent liabilities.

m. Engaging in hazardous lending and lax collection policies and practices, as evidenced by any of the following circumstances:

(1) An excessive volume of loans subject to adverse classification;

(2) An excessive volume of loans without adequate documentation, include credit information;

(3) Excessive net loan losses;

(4) An excessive volume of loans in relation to the total assets and deposit substitutes/trust liabilities of the QB/trust entity;

(5) An excessive volume of weak and self-serving loans to persons connected with the QB/trust entity, especially if a significant portion of these loans are adversely classified;

(6) Excessive concentrations of credit, especially if a substantial portion of this credit is adversely classified;

(7) Indiscriminate participation in weak and undocumented loans originated by other institutions;

(8) Failing to adopt written loan policies;

(9) An excessive volume of past due or NPLs;

(10) Failure to diversify the loan portfolio/asset mix of the institution;

(11) Failure to make provision for an adequate reserve for possible loan losses;

(12) High incidence of spurious and fraudulent loans due to patently inadequate risk management systems and procedures resulting in significant impairment of capital;

(13) QB's niche mostly consists of borrowers who have impaired or limited credit history, or majority of the loans are either clean/unsecured or backed with minimum collateral values except those underwritten using microfinance technology consistent with Sec. X361 and other acceptable cash flow-based lending systems; and the QB does not have a robust risk management system in place leaving the QB vulnerable to losses;

(14) Loan rates are excessively higher than market rates to compensate the added or higher risks involved. Excessively higher rates are those characterized by effective interest rates that are fifty percent (50%) over the prevailing comparable market median rate for similar loan types, maturities and collaterals; and

(15) Assignment of loans on without recourse basis with real estate properties as payment, resulting in total investment in real estate in excess of the prescribed ceiling.

n. Permitting officers to engage in lending practices beyond the scope of their positions.

o. Operating the QB/trust entity with inadequate internal controls.

p. Failure to keep accurate and updated books and records.

q. Operating the institution with excessive volume of out-of-territory loans.

r. Excessive volume of non-earning assets.

s. Failure to heed warnings and admonitions of the supervisory and regulatory authorities.

t. Continued and flagrant violation of any law, rule, regulation or written agreement between the institution and the BSP.

u. Any other action likely to cause insolvency or substantial dissipation of assets or earnings of the institution or likely to seriously weaken its condition or otherwise seriously prejudice the interest of its investors/clients.

v. Non-observance of the principles and the requirements for managing and monitoring large exposures and credit risk concentrations under Subsec. 4301Q.6a and b.

w. Improper or non-documentation of repurchase agreements covering government securities and commercial papers and other negotiable and non-negotiable securities or instruments.

(As amended by Circular No. 640 dated 16 January 2009)

REVISED IMPLEMENTING RULES AND REGULATIONS
R.A. NO. 9160, AS AMENDED BY R.A. NO. 9194
[Appendix to Sec. 4801Q (2008 - 4691Q)]

RULE 1
TITLE

Rule 1.a. Title. - These Rules shall be known and cited as the "Revised Rules and Regulations Implementing R.A. No. 9160", (the Anti-Money Laundering Act of 2001 [AMLA]), as amended by R.A. No. 9194.

Rule 1.b. Purpose. - These Rules are promulgated to prescribe the procedures and guidelines for the implementation of the AMLA, as amended by R.A. No. 9194.

RULE 2
DECLARATION OF POLICY

Rule 2. Declaration of Policy. - It is hereby declared the policy of the State to protect the integrity and confidentiality of bank accounts and to ensure that the Philippines shall not be used as a money-laundering site for the proceeds of any unlawful activity. Consistent with its foreign policy, the Philippines shall extend cooperation in transnational investigations and prosecutions of persons involved in money laundering activities wherever committed.

RULE 3
DEFINITIONS

Rule 3. Definitions. – For purposes of this Act, the following terms are hereby defined as follows:

Rule 3.a. *Covered Institution* refers to:

Rule 3.a.1. Banks, offshore banking units, quasi-banks, trust entities, non-stock savings and loan associations, pawnshops, and all other institutions, including their subsidiaries and affiliates supervised and/or regulated by the Bangko Sentral ng Pilipinas (BSP).

(a) A *subsidiary* means an entity more than fifty percent (50%) of the outstanding voting stock of which is owned by a bank, quasi-bank, trust entity or any other institution supervised or regulated by the BSP.

(b) An *affiliate* means an entity at least twenty percent (20%) but not exceeding fifty percent (50%) of the voting stock of which is owned by a bank, quasi-bank, trust entity, or any other institution supervised and/or regulated by the BSP.

Rule 3.a.2. Insurance companies, insurance agents, insurance brokers, professional reinsurers, reinsurance brokers, holding companies, holding company systems and all other persons and entities supervised and/or regulated by the Insurance Commission (IC).

(a) An *insurance company* includes those entities authorized to transact insurance business in the Philippines, whether life or non-life and whether domestic, domestically incorporated or branch of a foreign entity. A contract of insurance is an agreement whereby one undertakes for a consideration to indemnify another against loss, damage or liability arising from an unknown or contingent event. Transacting insurance business includes making or proposing to make, as insurer, any insurance contract, or as surety, any contract of suretyship as a vocation and not as merely incidental to any other legitimate business or activity of the surety, doing any kind of business specifically recognized as constituting the doing of an insurance business within the meaning of

Presidential Decree (P.D.) No. 612, as amended, including a reinsurance business and doing or proposing to do any business in substance equivalent to any of the foregoing in a manner designed to evade the provisions of P.D. No. 612, as amended.

(b) An *insurance agent* includes any person who solicits or obtains insurance on behalf of any insurance company or transmits for a person other than himself an application for a policy or contract of insurance to or from such company or offers or assumes to act in the negotiation of such insurance.

(c) An *insurance broker* includes any person who acts or aids in any manner in soliciting, negotiating or procuring the making of any insurance contract or in placing risk or taking out insurance, on behalf of an insured other than himself.

(d) A *professional reinsurer* includes any person, partnership, association or corporation that transacts solely and exclusively reinsurance business in the Philippines, whether domestic, domestically incorporated or a branch of a foreign entity. A contract of reinsurance is one by which an insurer procures a third person to insure him against loss or liability by reason of such original insurance.

(e) A *reinsurance broker* includes any person who, not being a duly authorized agent, employee or officer of an insurer in which any reinsurance is effected, acts or aids in any manner in negotiating contracts of reinsurance or placing risks of effecting reinsurance, for any insurance company authorized to do business in the Philippines.

(f) A *holding company* includes any person who directly or indirectly controls any authorized insurer. A holding company system includes a holding company together with its controlled insurers and controlled persons.

Rule 3.a.3. (i) Securities dealers, brokers, salesmen, associated persons of brokers or dealers, investment houses, investment agents and consultants, trading advisors, and other entities managing securities or rendering similar services, (ii) mutual funds or open-end investment companies, close-end investment companies, common trust funds, pre-need companies or issuers and other similar entities; (iii) foreign exchange corporations, money changers, money payment, remittance, and transfer companies and other similar entities, and (iv) other entities administering or otherwise dealing in currency, commodities or financial derivatives based thereon, valuable objects, cash substitutes and other similar monetary instruments or property supervised and/or regulated by the Securities and Exchange Commission (SEC).

(a) A *securities broker* includes a person engaged in the business of buying and selling securities for the account of others.

(b) A *securities dealer* includes any person who buys and sells securities for his/her account in the ordinary course of business.

(c) A *securities salesman* includes a natural person, employed as such or as an agent, by a dealer, issuer or broker to buy and sell securities.

(d) An *associated person of a broker or dealer* includes an employee thereof who directly exercises control or supervisory authority, but does not include a salesman, or an agent or a person whose functions are solely clerical or ministerial.

(e) An *investment house* includes an enterprise which engages or purports to engage, whether regularly or on an isolated basis, in the underwriting of securities of another person or enterprise, including securities of the Government and its instrumentalities.

(f) A *mutual fund or an open-end investment* company includes an investment company which is offering for sale or has outstanding, any redeemable security of which it is the issuer.

(g) A *closed-end investment company* includes an investment company other than open-end investment company.

(h) A *common trust fund* includes a fund maintained by an entity authorized to perform trust functions under a written and formally established plan, exclusively for the collective investment and reinvestment of certain money representing participation in the plan received by it in its capacity as trustee, for the purpose of administration, holding or management of such funds and/or properties for the use, benefit or advantage of the trustor or of others known as beneficiaries.

(i) A *pre-need company or issuer* includes any corporation supervised and/or regulated by the SEC and is authorized or licensed to sell or offer for sale pre-need plans. *Pre-need plans* are contracts which provide for the performance of future service(s) or payment of future monetary consideration at the time of actual need, payable either in cash or installment by the planholder at prices stated in the contract with or without interest or insurance coverage and includes life, pension, education, internment and other plans, which the Commission may, from time to time, approve.

(j) A *foreign exchange corporation* includes any enterprise which engages or purports to engage, whether regularly or on an isolated basis, in the sale and purchase of foreign currency notes and such other foreign-currency denominated non-bank deposit transactions as may be authorized under its articles of incorporation.

(k) *Investment Advisor/Agent/Consultant* shall refer to any person:

(1) who for an advisory fee is engaged in the business of advising others, either directly or through circulars, reports, publications or writings, as to the value of any security and as to the advisability of trading in any security; or

(2) who for compensation and as part of a regular business, issues or promulgates, analyzes reports concerning the capital market, except:

(a) any bank or trust company;

(b) any journalist, reporter, columnist, editor, lawyer, accountant, teacher;

(c) the publisher of any bonafide newspaper, news, business or financial publication of general and regular circulation, including their employees;

(d) any contract market;

(e) such other person not within the intent of this definition, provided that the furnishing of such service by the foregoing persons is solely incidental to the conduct of their business or profession.

(3) any person who undertakes the management of portfolio securities of investment companies, including the arrangement of purchases, sales or exchanges of securities.

(l) A *moneychanger* includes any person in the business of buying or selling foreign currency notes.

(m) A *money payment, remittance and transfer company* includes any person offering to pay, remit or transfer or transmit money on behalf of any person to another person.

(n) *"Customer"* refers to any person or entity that keeps an account, or otherwise transacts business, with a covered institution and any person or entity on whose behalf an account is maintained or a transaction is conducted, as well as the beneficiary of said transactions. A customer also includes the beneficiary of a trust, an investment fund, a pension fund or a company or person whose assets are managed by an asset manager, or a grantor of a trust. It includes any insurance policy holder, whether actual or prospective.

(o) *"Property"* includes any thing or item of value, real or personal, tangible or intangible, or any interest therein or any benefit, privilege, claim or right with respect thereto.

Rule 3.b. *Covered transaction* is a transaction in cash or other equivalent monetary instrument involving a total amount in excess of PhP500,000.00 within one (1) banking day.

Rule 3.b.1. *Suspicious transactions* are transactions, regardless of amount, where any of the following circumstances exists:

(1) There is no underlying legal or trade obligation, purpose or economic justification;

(2) The client is not properly identified;

(3) The amount involved is not commensurate with the business or financial capacity of the client;

(4) Taking into account all known circumstances, it may be perceived that the client's transaction is structured in order to avoid being the subject of reporting requirements under the act;

(5) Any circumstance relating to the transaction which is observed to deviate from the profile of the client and/or the client's past transactions with the covered institution;

(6) The transaction is in any way related to an unlawful activity or any money laundering activity or offense under this act that is about to be, is being or has been committed; or

(7) Any transaction that is similar, analogous or identical to any of the foregoing.

Rule 3.c. *Monetary instrument* refers to:

(1) Coins or currency of legal tender of the Philippines, or of any other country;

(2) Drafts, checks and notes;

(3) Securities or negotiable instruments, bonds, commercial papers, deposit certificates, trust certificates, custodial receipts or deposit substitute instruments, trading orders, transaction tickets and confirmations of sale or investments and money market instruments;

(4) Contracts or policies of insurance, life or non-life, and contracts of suretyship; and

(5) Other similar instruments where title thereto passes to another by endorsement, assignment or delivery.

Rule 3.d. *Offender* refers to any person who commits a money laundering offense.

Rule 3.e. *Person* refers to any natural or juridical person.

Rule 3.f. *Proceeds* refers to an amount derived or realized from an unlawful activity. It includes:

(1) All material results, profits, effects and any amount realized from any unlawful activity;

(2) All monetary, financial or economic means, devices, documents, papers or things used in or having any relation to any unlawful activity; and

(3) All moneys, expenditures, payments, disbursements, costs, outlays, charges, accounts, refunds and other similar items for the financing, operations, and maintenance of any unlawful activity.

Rule 3.g. *Supervising authority* refers to the BSP, the SEC and the IC. Where the BSP, SEC or IC supervision applies only to the registration of the covered institution, the BSP, the SEC or the IC, within the limits of the AMLA, shall have the authority to require and ask assistance from the government agency having regulatory power and/or licensing authority over said covered institution for the implementation and enforcement of the AMLA and these Rules.

Rule 3.h. *Transaction* refers to any act establishing any right or obligation or giving rise to any contractual or legal relationship between the parties thereto. It also includes any movement of funds by any means with a covered institution.

Rule 3.i. *Unlawful activity* refers to any act or omission or series or combination thereof involving or having relation, to the following:

(A) Kidnapping for ransom under Article 267 of Act No. 3815, otherwise known as the Revised Penal Code, as amended;

(1) Kidnapping for ransom

(B) Sections 4, 5, 6, 8, 9, 10, 12, 13, 14, 15 and 16 of R.A. No. 9165, otherwise known as the Comprehensive Dangerous Drugs Act of 2002;

(2) Importation of prohibited drugs;
(3) Sale of prohibited drugs;
(4) Administration of prohibited drugs;
(5) Delivery of prohibited drugs
(6) Distribution of prohibited drugs
(7) Transportation of prohibited drugs
(8) Maintenance of a Den, Dive or Resort for prohibited users
(9) Manufacture of prohibited drugs
(10)Possession of prohibited drugs
(11)Use of prohibited drugs
(12)Cultivation of plants which are sources of prohibited drugs
(13)Culture of plants which are sources of prohibited drugs

(C) Section 3 paragraphs b, c, e, g, h and i of R.A. No. 3019, as amended, otherwise known as the Anti-Graft and Corrupt Practices Act;

(14)Directly or indirectly requesting or receiving any gift, present, share, percentage or benefit for himself or for any other person in connection with any contract or transaction between the Government and any party, wherein the public officer in his official capacity has to intervene under the law;

(15) Directly or indirectly requesting or receiving any gift, present or other pecuniary or material benefit, for himself or for another, from any person for whom the public officer, in any manner or capacity, has secured or obtained, or will secure or obtain, any government permit or license, in consideration for the help given or to be given, without prejudice to Section 13 of R.A. No. 3019;

(16) Causing any undue injury to any party, including the government, or giving any private party any unwarranted benefits, advantage or preference in the discharge of his official, administrative or judicial functions through manifest partiality, evident bad faith or gross inexcusable negligence;

(17) Entering, on behalf of the government, into any contract or transaction manifestly and grossly disadvantageous to the same, whether or not the public officer profited or will profit thereby;

(18) Directly or indirectly having financial or pecuniary interest in any business contract or transaction in connection with which he intervenes or takes part in his official capacity, or in which he is prohibited by the Constitution or by any law from having any interest;

(19) Directly or indirectly becoming interested, for personal gain, or having material interest in any transaction or act requiring the approval of a board, panel or group of which he is a member, and which exercise of discretion in such approval, even if he votes against the same or he does not participate in the action of the board, committee, panel or group.

(D) Plunder under R.A. No. 7080, as amended;

(20) Plunder through misappropriation, conversion, misuse or malversation of

public funds or raids upon the public treasury;

(21) Plunder by receiving, directly or indirectly, any commission, gift, share, percentage, kickbacks or any other form of pecuniary benefit from any person and/or entity in connection with any government contract or project or by reason of the office or position of the public officer concerned;

(22) Plunder by the illegal or fraudulent conveyance or disposition of assets belonging to the National Government or any of its subdivisions, agencies, instrumentalities or government-owned or controlled corporations or their subsidiaries;

(23) Plunder by obtaining, receiving or accepting, directly or indirectly, any shares of stock, equity or any other form of interest or participation including the promise of future employment in any business enterprise or undertaking;

(24) Plunder by establishing agricultural, industrial or commercial monopolies or other combinations and/or implementation of decrees and orders intended to benefit particular persons or special interests;

(25) Plunder by taking undue advantage of official position, authority, relationship, connection or influence to unjustly enrich himself or themselves at the expense and to the damage and prejudice of the Filipino people and the republic of the Philippines.

(E) Robbery and extortion under Articles 294, 295, 296, 299, 300, 301 and 302 of the Revised Penal Code, as amended;

(26) Robbery with violence or intimidation of persons;

(27) Robbery with physical injuries, committed in an uninhabited place and by a band, or with use of firearms on a street, road or alley;

(28) Robbery in an uninhabited house or public building or edifice devoted to worship.

(F) Jueteng and Masiao punished as illegal gambling under P.D. No. 1602;

(29) Jueteng;

(30) Masiao.

(G) Piracy on the high seas under the Revised Penal Code, as amended and P.D. No. 532;

(31) Piracy on the high seas;

(32) Piracy in inland Philippine waters;

(33) Aiding and abetting pirates and brigands.

(H) Qualified theft under Article 310 of the Revised Penal Code, as amended;

(34) Qualified theft.

(I) Swindling under Article 315 of the Revised Penal Code, as amended;

(35) Estafa with unfaithfulness or abuse of confidence by altering the substance, quality or quantity of anything of value which the offender shall deliver by virtue of an obligation to do so, even though such obligation be based on an immoral or illegal consideration;

(36) Estafa with unfaithfulness or abuse of confidence by misappropriating or converting, to the prejudice of another, money, goods or any other personal property received by the offender in trust or on commission, or for administration, or under any other obligation involving the duty to make delivery or to return the same, even though such obligation be totally or partially guaranteed by a bond; or by denying having received such money, goods, or other property;

(37) Estafa with unfaithfulness or abuse of confidence by taking undue advantage of the signature of the offended party in blank, and by writing any document above such signature in blank, to the prejudice of the offended party or any third person;

(38) Estafa by using a fictitious name, or falsely pretending to possess power, influence, qualifications, property, credit,

agency, business or imaginary transactions, or by means of other similar deceits;

(39) Estafa by altering the quality, fineness or weight of anything pertaining to his art or business;

(40) Estafa by pretending to have bribed any government employee;

(41) Estafa by postdating a check, or issuing a check in payment of an obligation when the offender has no funds in the bank, or his funds deposited therein were not sufficient to cover the amount of the check;

(42) Estafa by inducing another, by means of deceit, to sign any document;

(43) Estafa by resorting to some fraudulent practice to ensure success in a gambling game;

(44) Estafa by removing, concealing or destroying, in whole or in part, any court record, office files, document or any other papers.

(J) Smuggling under R.A. Nos. 455 and 1937;

(45) Fraudulent importation of any vehicle;

(46) Fraudulent exportation of any vehicle;

(47) Assisting in any fraudulent importation;

(48) Assisting in any fraudulent exportation;

(49) Receiving smuggled article after fraudulent importation;

(50) Concealing smuggled article after fraudulent importation;

(51) Buying smuggled article after fraudulent importation;

(52) Selling smuggled article after fraudulent importation;

(53) Transportation of smuggled article after fraudulent importation;

(54) Fraudulent practices against customs revenue.

(K) Violations under R.A. No. 8792, otherwise known as the Electronic Commerce Act of 2000;

K.1. *Hacking or cracking*, which refers to:

(55) unauthorized access into or interference in a computer system/server or information and communication system; or

(56) any access in order to corrupt, alter, steal, or destroy using a computer or other similar information and communication devices, without the knowledge and consent of the owner of the computer or information and communications system, including

(57) the introduction of computer viruses and the like, resulting in the corruption, destruction, alteration, theft or loss of electronic data messages or electronic document;

K.2. *Piracy*, which refers to:

(58) the unauthorized copying, reproduction,

(59) the unauthorized dissemination, distribution,

(60) the unauthorized importation,

(61) the unauthorized use, removal, alteration, substitution, modification,

(62) the unauthorized storage, uploading, downloading, communication, making available to the public, or

(63) the unauthorized broadcasting, of protected material, electronic signature or copyrighted works including legally protected sound recordings or phonograms or information material on protected works, through the use of telecommunication networks, such as, but not limited to, the internet, in a manner that infringes intellectual property rights;

K.3. Violations of the Consumer Act or R.A. No. 7394 and other relevant or pertinent laws through transactions covered by or using electronic data messages or electronic documents:

(64) Sale of any consumer product that is not in conformity with standards under the Consumer Act;

(65) Sale of any product that has been banned by a rule under the Consumer Act;

(66) Sale of any adulterated or mislabeled product using electronic documents;

(67) Adulteration or misbranding of any consumer product;

(68) Forging, counterfeiting or simulating any mark, stamp, tag, label or other identification device;

(69) Revealing trade secrets;

(70) Alteration or removal of the labeling of any drug or device held for sale;

(71) Sale of any drug or device not registered in accordance with the provisions of the E-Commerce Act;

(72) Sale of any drug or device by any person not licensed in accordance with the provisions of the E-Commerce Act;

(73) Sale of any drug or device beyond its expiration date;

(74) Introduction into commerce of any mislabeled or banned hazardous substance;

(75) Alteration or removal of the labeling of a hazardous substance;

(76) Deceptive sales acts and practices;

(77) Unfair or unconscionable sales acts and practices;

(78) Fraudulent practices relative to weights and measures;

(79) False representations in advertisements as the existence of a warranty or guarantee;

(80) Violation of price tag requirements;

(81) Mislabeling consumer products;

(82) False, deceptive or misleading advertisements;

(83) Violation of required disclosures on consumer loans;

(84) Other violations of the provisions of the E-Commerce Act;

(L) Hijacking and other violations under R.A. No. 6235; destructive arson and murder, as defined under the Revised Penal Code, as amended, including those perpetrated by terrorists against non-combatant persons and similar targets;

(85) Hijacking;

(86) Destructive arson;

(87) Murder;

(88) Hijacking, destructive arson or murder perpetrated by terrorists against non-combatant persons and similar targets;

(M) Fraudulent practices and other violations under R.A. No. 8799, otherwise known as the Securities Regulation Code of 2000;

(89) Sale, offer or distribution of securities within the Philippines without a registration statement duly filed with and approved by the SEC;

(90) Sale or offer to the public of any pre-need plan not in accordance with the rules and regulations which the SEC shall prescribe;

(91) Violation of reportorial requirements imposed upon issuers of securities;

(92) Manipulation of security prices by creating a false or misleading appearance of active trading in any listed security traded in an Exchange or any other trading market;

(93) Manipulation of security prices by effecting, alone or with others, a series of transactions in securities that raises their prices to induce the purchase of a security, whether of the same or different class, of the same issuer or of a controlling, controlled or commonly controlled company by others;

(94) Manipulation of security prices by effecting, alone or with others, a series of transactions in securities that depresses their price to induce the sale of a security, whether of the same or different class, of the same issuer or of a controlling, controlled or commonly controlled company by others;

(95) Manipulation of security prices by effecting, alone or with others, a series of transactions in securities that creates active trading to induce such a purchase or sale though manipulative devices such as marking the close, painting the tape, squeezing the float, hype and dump, boiler room operations and such other similar devices;

(96) Manipulation of security prices by circulating or disseminating information that the price of any security listed in an Exchange will or is likely to rise or fall because of manipulative market operations of any one or more persons conducted for the purpose of raising or depressing the price of the security for the purpose of inducing the purchase or sale of such security;

(97) Manipulation of security prices by making false or misleading statements with respect to any material fact, which he knew or had reasonable ground to believe was so false and misleading, for the purpose of inducing the purchase or sale of any security listed or traded in an Exchange;

(98) Manipulation of security prices by effecting, alone or with others, any series of transactions for the purchase and/or sale of any security traded in an Exchange for the purpose of pegging, fixing or stabilizing the price of such security, unless otherwise allowed by the Securities Regulation Code or by the rules of the SEC;

(99) Sale or purchase of any security using any manipulative deceptive device or contrivance;

(100) Execution of short sales or stop-loss order in connection with the purchase or sale of any security not in accordance with such rules and regulations as the SEC may prescribe as necessary and appropriate in the public interest or the protection of the investors;

(101) Employment of any device, scheme or artifice to defraud in connection with the purchase and sale of any securities;

(102) Obtaining money or property in connection with the purchase and sale of any security by means of any untrue statement of a material fact or any omission to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading;

(103) Engaging in any act, transaction, practice or course of action in the sale and purchase of any security which operates or would operate as a fraud or deceit upon any person;

(104) Insider trading;

(105) Engaging in the business of buying and selling securities in the Philippines as a broker or dealer, or acting as a salesman, or an associated person of any broker or dealer without any registration from the Commission;

(106) Employment by a broker or dealer of any salesman or associated person or by an issuer of any salesman, not registered with the SEC;

(107) Effecting any transaction in any security, or reporting such transaction, in an Exchange or using the facility of an Exchange which is not registered with the SEC;

(108) Making use of the facility of a clearing agency which is not registered with the SEC;

(109) Violations of margin requirements;

(110) Violations on the restrictions on borrowings by members, brokers and dealers;

(111) Aiding and Abetting in any violations of the Securities Regulation Code;

(112) Hindering, obstructing or delaying the filing of any document required under the Securities Regulation Code or the rules and regulations of the SEC;

(113) Violations of any of the provisions of the implementing rules and regulations of the SEC;

(114) Any other violations of any of the provisions of the Securities Regulation Code.

(N) Felonies or offenses of a similar nature to the afore-mentioned unlawful activities that are punishable under the penal laws of other countries.

In determining whether or not a felony or offense punishable under the penal laws of other countries, is "of a similar nature", as to constitute the same as an unlawful activity under the AMLA, the nomenclature of said felony or offense need not be identical to any of the predicate crimes listed under Rule 3.i.

RULE 4
MONEY LAUNDERING OFFENSE

Rule 4.1. Money Laundering Offense. - Money laundering is a crime whereby the proceeds of an unlawful activity as herein defined are transacted, thereby making them appear to have originated from legitimate sources. It is committed by the following:

(a) Any person knowing that any monetary instrument or property represents, involves, or relates to, the proceeds of any unlawful activity, transacts or attempts to transact said monetary instrument or property.

(b) Any person knowing that any monetary instrument or property involves the proceeds of any unlawful activity, performs or fails to perform any act as a result of which he facilitates the offense of money laundering referred to in paragraph (a) above.

(c) Any person knowing that any monetary instrument or property is required under this Act to be disclosed and filed with the Anti-Money Laundering Council (AMLC), fails to do so.

RULE 5
JURISDICTION OF MONEY LAUNDERING CASES AND MONEY LAUNDERING INVESTIGATION PROCEDURES

Rule 5.1. Jurisdiction of Money Laundering Cases. - The Regional Trial Courts shall have the jurisdiction to try all cases on money laundering. Those committed by public officers and private persons who are in conspiracy with such public officers shall be under the jurisdiction of the Sandiganbayan.

Rule 5.2. Investigation of Money Laundering Offenses. - The AMLC shall investigate:

(a) Suspicious transactions;

(b) Covered transactions deemed suspicious after an investigation conducted by the AMLC;

(c) Money laundering activities; and

(d) Other violations of this act.

Rule 5.3. Attempts at Transactions. - Section 4 (a) and (b) of the AMLA provides that any person who attempts to transact any monetary instrument or property representing, involving or relating to the proceeds of any unlawful activity shall be prosecuted for a money laundering offense. Accordingly, the reports required under Rule 9.3 (a) and (b) of these Rules shall include those pertaining to any attempt by any person to transact any monetary instrument or property representing, involving or relating to the proceeds of any unlawful activity.

RULE 6
PROSECUTION OF MONEY LAUNDERING

Rule 6.1. Prosecution of Money Laundering

(a) Any person may be charged with and convicted of both the offense of money

laundering and the unlawful activity as defined under Rule 3 (i) of the AMLA.

(b) Any proceeding relating to the unlawful activity shall be given precedence over the prosecution of any offense or violation under the AMLA without prejudice to the application *Ex-Parte* by the AMLC to the Court of Appeals for a Freeze Order with respect to the monetary instrument or property involved therein and resort to other remedies provided under the AMLA, the rules of court and other pertinent laws and rules.

Rule 6.2. When the AMLC finds, after investigation, that there is probable cause to charge any person with a money laundering offense under Section 4 of the AMLA, it shall cause a complaint to be filed, pursuant to Section 7 (4) of the AMLA, before the Department of Justice or the Ombudsman, which shall then conduct the preliminary investigation of the case.

Rule 6.3. After due notice and hearing in the preliminary investigation proceedings before the Department of Justice, or the Ombudsman, as the case may be, and the latter should find probable cause of a money laundering offense, it shall file the necessary information before the Regional Trial Courts or the Sandiganbayan.

Rule 6.4. Trial for the money laundering offense shall proceed in accordance with the Code of Criminal Procedure or the Rules of Procedure of the Sandiganbayan, as the case may be.

Rule 6.5. Knowledge of the offender that any monetary instrument or property represents, involves, or relates to the proceeds of an unlawful activity or that any monetary instrument or property is required under the AMLA to be disclosed and filed with the AMLC, may be established by direct evidence or inferred from the attendant circumstances.

Rule 6.6. All the elements of every money laundering offense under Section 4 of the AMLA must be proved by evidence beyond reasonable doubt, including the element of knowledge that the monetary instrument or property represents, involves or relates to the proceeds of any unlawful activity.

Rule 6.7. No element of the unlawful activity, however, including the identity of the perpetrators and the details of the actual commission of the unlawful activity need be established by proof beyond reasonable doubt. The elements of the offense of money laundering are separate and distinct from the elements of the felony or offense constituting the unlawful activity.

RULE 7
CREATION OF ANTI-MONEY LAUNDERING COUNCIL (AMLC)

Rule 7.1.a. Composition. - The Anti-Money Laundering Council is hereby created and shall be composed of the Governor of the BSP as Chairman, the Commissioner of the Insurance Commission and the Chairman of the SEC as members.

Rule 7.1.b. Unanimous Decision. - The AMLC shall act unanimously in discharging its functions as defined in the AMLA and in these Rules. However, in the case of the incapacity, absence or disability of any member to discharge his functions, the officer duly designated or authorized to discharge the functions of the Governor of the BSP, the Chairman of the SEC or the Insurance Commissioner, as the case may be, shall act in his stead in the AMLC.

Rule 7.2. Functions. - The functions of the AMLC are defined hereunder:

(1) to require and receive covered or suspicious transaction reports from covered institutions;

(2) to issue orders addressed to the appropriate Supervising Authority or the covered institution to determine the true identity of the owner of any monetary instrument or property subject of a covered or suspicious transaction report, or request for assistance from a foreign State, or believed by the Council, on the basis of substantial evidence, to be, in whole or in part, wherever located, representing, involving, or related to, directly or indirectly, in any manner or by any means, the proceeds of an unlawful activity;

(3) to institute civil forfeiture proceedings and all other remedial proceedings through the Office of the Solicitor General;

(4) to cause the filing of complaints with the Department of Justice or the Ombudsman for the prosecution of money laundering offenses;

(5) to investigate suspicious transactions and covered transactions deemed suspicious after an investigation by the AMLC, money laundering activities and other violations of this Act;

(6) to apply before the Court of Appeals, Ex-Parte, for the freezing of any monetary instrument or property alleged to be proceeds of any unlawful activity as defined under Section 3(i) hereof;

(7) to implement such measures as may be inherent, necessary, implied, incidental and justified under the AMLA to counteract money laundering. Subject to such limitations as provided for by law, the AMLC is authorized under Rule 7 (7) of the AMLA to establish an information sharing system that will enable the AMLC to store, track and analyze money laundering transactions for the resolute prevention, detection and investigation of money laundering offenses. For this purpose, the AMLC shall install a computerized system that will be used in the creation and maintenance of an information database;

(8) to receive and take action in respect of any request from foreign states for assistance in their own anti-money laundering operations as provided in the AMLA. The AMLC is authorized under Sections 7 (8) and 13 (b) and (d) of the AMLA to receive and take action in respect of any request of foreign states for assistance in their own anti-money laundering operations, in respect of conventions, resolutions and other directives of the United Nations (UN), the UN Security Council, and other international organizations of which the Philippines is a member. However, the AMLC may refuse to comply with any such request, convention, resolution or directive where the action sought therein contravenes the provisions of the Constitution, or the execution thereof is likely to prejudice the national interest of the Philippines.

(9) to develop educational programs on the pernicious effects of money laundering, the methods and techniques used in money laundering, the viable means of preventing money laundering and the effective ways of prosecuting and punishing offenders.

(10) to enlist the assistance of any branch, department, bureau, office, agency or instrumentality of the government, including government-owned and -controlled corporations, in undertaking any and all anti-money laundering operations, which may include the use of its personnel, facilities and resources for the more resolute prevention, detection and investigation of money laundering offenses and prosecution of offenders. The AMLC may require the intelligence units of the Armed Forces of the Philippines, the Philippine National Police, the Department of Finance, the Department of Justice, as well as their attached agencies, and other domestic or transnational governmental or non-governmental organizations or groups to divulge to the AMLC all information that may, in any way, facilitate the resolute prevention,

investigation and prosecution of money laundering offenses and other violations of the AMLA.

(11) To impose administrative sanctions for the violation of laws, rules, regulations and orders and resolutions issued pursuant thereto.

Rule 7.3. Meetings. - The AMLC shall meet every first Monday of the month, or as often as may be necessary at the call of the Chairman.

RULE 8
CREATION OF A SECRETARIAT

Rule 8.1. The Executive Director. - The Secretariat shall be headed by an Executive Director who shall be appointed by the AMLC for a term of five (5) years. He must be a member of the Philippine Bar, at least thirty-five (35) years of age, must have served at least five (5) years either at the BSP, the SEC or the IC and of good moral character, unquestionable integrity and known probity. He shall be considered a regular employee of the BSP with the rank of Assistant Governor, and shall be entitled to such benefits and subject to such rules and regulations, as well as prohibitions, as are applicable to officers of similar rank.

Rule 8.2. Composition. - In organizing the Secretariat, the AMLC may choose from those who have served, continuously or cumulatively, for at least five (5) years in the BSP, the SEC or the IC. All members of the Secretariat shall be considered regular employees of the BSP and shall be entitled to such benefits and subject to such rules and regulations as are applicable to BSP employees of similar rank.

Rule 8.3. Detail and Secondment. - The AMLC is authorized under Section 7 (10) of the AMLA to enlist the assistance of the BSP, the SEC or the IC, or any other branch, department, bureau, office, agency or instrumentality of the government, including government-owned and controlled corporations, in undertaking any and all anti-money laundering operations. This includes the use of any member of their personnel who may be detailed or seconded to the AMLC, subject to existing laws and Civil Service Rules and Regulations. Detailed personnel shall continue to receive their salaries, benefits and emoluments from their respective mother units. Seconded personnel shall receive, in lieu of their respective compensation packages from their respective mother units, the salaries, emoluments and all other benefits to which their AMLC Secretariat positions are entitled to.

Rule 8.4. Confidentiality Provisions. - The members of the AMLC, the Executive Director, and all the members of the Secretariat, whether permanent, on detail or on secondment, shall not reveal, in any manner, any information known to them by reason of their office. This prohibition shall apply even after their separation from the AMLA. In case of violation of this provision, the person shall be punished in accordance with the pertinent provisions of the Central Bank Act.

RULE 9
PREVENTION OF MONEY LAUNDERING; CUSTOMER IDENTIFICATION REQUIREMENTS AND RECORD KEEPING

Rule 9.1. Customer Identification Requirements

Rule 9.1.a. Customer Identification. - Covered institutions shall establish and record the true identity of its clients based on official documents. They shall maintain a system of verifying the true identity of their clients and, in case of corporate clients, require a system of

verifying their legal existence and organizational structure, as well as the authority and identification of all persons purporting to act on their behalf. Covered institutions shall establish appropriate systems and methods based on internationally compliant standards and adequate internal controls for verifying and recording the true and full identity of their customers.

Rule 9.1.b. Trustee, Nominee and Agent Accounts. - When dealing with customers who are acting as trustee, nominee, agent or in any capacity for and on behalf of another, covered institutions shall verify and record the true and full identity of the person(s) on whose behalf a transaction is being conducted. Covered institutions shall also establish and record the true and full identity of such trustees, nominees, agents and other persons and the nature of their capacity and duties. In case a covered institution has doubts as to whether such persons are being used as dummies in circumvention of existing laws, it shall immediately make the necessary inquiries to verify the status of the business relationship between the parties.

Rule 9.1.c. Minimum Information/ Documents Required for Individual Customers. - Covered institutions shall require customers to produce original documents of identity issued by an official authority, bearing a photograph of the customer. Examples of such documents are identity cards and passports. The following minimum information/documents shall be obtained from individual customers:

(1) Name;
(2) Present address;
(3) Permanent address;
(4) Date and place of birth;
(5) Nationality;
(6) Nature of work and name of employer or nature of self-employment/ business;
(7) Contact numbers;
(8) Tax identification number, Social Security System number or Government Service and Insurance System number;
(9) Specimen signature;
(10) Source of fund(s); and
(11) Names of beneficiaries in case of insurance contracts and whenever applicable.

Rule 9.1.d. Minimum Information/ Documents Required for Corporate and Juridical Entities. - Before establishing business relationships, covered institutions shall endeavor to ensure that the customer is a corporate or juridical entity which has not been or is not in the process of being, dissolved, wound up or voided, or that its business or operations has not been or is not in the process of being, closed, shut down, phased out, or terminated. Dealings with shell companies and corporations, being legal entities which have no business substance in their own right but through which financial transactions may be conducted, should be undertaken with extreme caution. The following minimum information/ documents shall be obtained from customers that are corporate or juridical entities, including shell companies and corporations:

(1) Articles of Incorporation/ Partnership;
(2) By-laws;
(3) Official address or principal business address;
(4) List of directors/partners;
(5) List of principal stockholders owning at least two percent (2%) of the capital stock;
(6) Contact numbers;
(7) Beneficial owners, if any; and
(8) Verification of the authority and identification of the person purporting to act on behalf of the client.

Rule 9.1.e. Prohibition Against Certain Accounts. Covered institutions shall maintain accounts only in the true and full name of the account owner or holder. The provisions of existing laws to the contrary notwithstanding, anonymous accounts, accounts under fictitious names, and all other similar accounts shall be absolutely prohibited.

Rule 9.1.f. Prohibition Against Opening of Accounts Without Face-to-face Contact. - No new accounts shall be opened and created without face-to-face contact and full compliance with the requirements under Rule 9.1.c of these Rules.

Rule 9.1.g. Numbered Accounts. - Peso and foreign currency non-checking numbered accounts shall be allowed: *Provided*, That the true identity of the customers of all peso and foreign currency non-checking numbered accounts are satisfactorily established based on official and other reliable documents and records, and that the information and documents required under the provisions of these Rules are obtained and recorded by the covered institution. No peso and foreign currency non-checking accounts shall be allowed without the establishment of such identity and in the manner herein provided. The BSP may conduct annual testing for the purpose of determining the existence and true identity of the owners of such accounts. The SEC and the IC may conduct similar testing more often than once a year and covering such other related purposes as may be allowed under their respective charters.

Rule 9.2. Record Keeping Requirements

Rule 9.2.a. Record Keeping: Kinds of Records and Period for Retention. – All records of all transactions of covered institutions shall be maintained and safely stored for five (5) years from the dates of transactions. Said records and files shall contain the full and true identity of the owners or holders of the accounts involved in the covered transactions and all other customer identification documents. Covered institutions shall undertake the necessary adequate security measures to ensure the confidentiality of such file. Covered institutions shall prepare and maintain documentation, in accordance with the aforementioned client identification requirements, on their customer accounts, relationships and transactions such that any account, relationship or transaction can be so reconstructed as to enable the AMLC, and/or the courts to establish an audit trail for money laundering.

Rule 9.2.b. Existing and New Accounts and New Transactions. - All records of existing and new accounts and of new transactions shall be maintained and safely stored for five (5) years from 17 October 2001 or from the dates of the accounts or transactions, whichever is later.

Rule 9.2.c. Closed Accounts. - With respect to closed accounts, the records on customer identification, account files and business correspondence shall be preserved and safely stored for at least five (5) years from the dates when they were closed.

Rule 9.2.d. Retention of Records in Case a Money Laundering Case has been Filed in Court. – If a money laundering case based on any record kept by the covered institution concerned has been filed in court, said file must be retained beyond the period stipulated in the three (3) immediately preceding sub-Rules, as the case may be, until it is confirmed that the case has been finally resolved or terminated by the court.

Rule 9.2.e. Form of Records. – Records shall be retained as originals in such forms as are admissible in court pursuant to

existing laws and the applicable rules promulgated by the Supreme Court.

Rule 9.3. Reporting of Covered Transactions. -

Rule 9.3.a. Period of Reporting Covered Transactions and SuspiciousTransactions. - Covered institutions shall report to the AMLC all covered transactions and suspicious transactions within five (5) working days from occurrence thereof, unless the supervising authority concerned prescribes a longer period not exceeding ten (10) working days.

Should a transaction be determined to be both a covered and a suspicious transaction, the covered institution shall report the same as a suspicious transaction.

The reporting of covered transactions by covered institutions shall be deferred for a period of sixty (60) days after the effectivity of R.A. No. 9194, or as may be determined by the AMLC, in order to allow the covered institutions to configure their respective computer systems; provided that, all covered transactions during said deferment period shall be submitted thereafter.

Rule 9.3.b. Covered* and Suspicious *Transaction Report Forms. - The Covered Transaction Report (CTR) and the Suspicious Transaction Report (STR) shall be in the forms prescribed by the AMLC.

Rule 9.3.b.1. Covered institutions shall use the existing forms for Covered Transaction Reports and Suspicious Transaction Reports, until such time as the AMLC has issued new sets of forms.

Rule 9.3.b.2. Covered Transaction Reports and Suspicious Transaction Reports shall be submitted in a secured manner to the AMLC in electronic form, either via diskettes, leased lines, or through internet facilities, with the corresponding hard copy for suspicious transactions. The final flow and procedures for such reporting shall be mapped out in the manual of operations to be issued by the AMLC.

Rule 9.3.c. Exemption from Bank Secrecy Laws. – When reporting covered or suspicious transactions to the AMLC, covered institutions and their officers and employees, shall not be deemed to have violated R.A. No. 1405, as amended, R.A. No. 6426, as amended, R.A. No. 8791 and other similar laws, but are prohibited from communicating, directly or indirectly, in any manner or by any means, to any person the fact that a covered or suspicious transaction report was made, the contents thereof, or any other information in relation thereto. In case of violation thereof, the concerned officer and employee of the covered institution, shall be criminally liable.

Rule 9.3.d. Confidentiality Provisions. – When reporting covered transactions or suspicious transactions to the AMLC, covered institutions and their officers, employees, representatives, agents, advisors, consultants or associates are prohibited from communicating, directly or indirectly, in any manner or by any means, to any person, entity, or the media, the fact that a covered transaction report was made, the contents thereof, or any other information in relation thereto. Neither may such reporting be published or aired in any manner or form by the mass media, electronic mail, or other similar devices. In case of violation hereof, the concerned officer, employee, representative, agent, advisor, consultant or associate of the covered institution, or media shall be held criminally liable.

Rule 9.3.e. *Safe Harbor Provisions.* – No administrative, criminal or civil proceedings, shall lie against any person for having made a covered transaction report or a suspicious transaction report in the regular performance of his duties and in good faith, whether or not such reporting results in any criminal prosecution under this Act or any other Philippine law.

RULE 10
APPLICATION FOR FREEZE ORDERS

Rule 10.1. When the AMLC May Apply for the Freezing of Any Monetary Instrument or Property. -

(a) After an investigation conducted by the AMLC and upon determination that probable cause exists that a monetary instrument or property is in any way related to any unlawful activity as defined under Section 3 (i), the AMLC may file an Ex-Parte application before the Court of Appeals for the issuance of a freeze order on any monetary instrument or property subject thereof prior to the institution or in the course of, the criminal proceedings involving the unlawful activity to which said monetary instrument or property is any way related.

(b) Considering the intricate and diverse web of related and interlocking accounts pertaining to the monetary instrument(s) or property(ies) that any person may create in the different covered institutions, their branches and/or other units, the AMLC may apply to the Court of Appeals for the freezing, not only of the monetary instruments or properties in the names of the reported owner(s)/holder(s), and monetary instruments or properties named in the application of the AMLC but also all other related web of accounts pertaining to other monetary instruments and properties, the funds and sources of which originated from or are related to the monetary instrument(s) or property(ies) subject of the freeze order(s).

(c) The freeze order shall be effective for twenty (20) days unless extended by the Court of Appeals upon application by the AMLC.

Rule 10.2. Definition of Probable Cause. - Probable cause includes such facts and circumstances which would lead a reasonably discreet, prudent or cautious man to believe that an unlawful activity and/or a money laundering offense is about to be, is being or has been committed and that the account or any monetary instrument or property subject thereof sought to be frozen is in any way related to said unlawful activity and/or money laundering offense.

Rule 10.3. Duty of Covered Institution Upon Receipt Thereof. –

Rule 10.3.a. Upon receipt of the notice of the freeze order, the covered institution concerned shall immediately freeze the monetary instrument or property and related web of accounts subject thereof.

Rule 10.3.b. The covered institution shall likewise immediately furnish a copy of the notice of the freeze order upon the owner or holder of the monetary instrument or property or related web of accounts subject thereof.

Rule 10.3.c. Within twenty-four (24) hours from receipt of the freeze order, the covered institution concerned shall submit to the Court of Appeals and the AMLC, by personal delivery, a detailed written return on the freeze order, specifying all the pertinent and relevant information which shall include the following:

1. The account number(s);
2. The name(s) of the account owner(s) or holder(s);
3. The amount of the monetary instrument, property or related web of accounts as of the time they were frozen;

4. All relevant information as to the nature of the monetary instrument or property;

5. Any information on the related web of accounts pertaining to the monetary instrument or property subject of the freeze order; and

6. The time when the freeze thereon took effect.

Rule 10.4. Definition of Related Web of Accounts. -

Related Web of Accounts pertaining to the money instrument or property subject of the freeze order is defined as those accounts, the funds and sources of which originated from and/or are materially linked to the monetary instrument(s) or property(ies) subject of the freeze order(s).

Upon receipt of the freeze order issued by the court of appeals and upon verification by the covered institution that the related web of accounts originated from and/or are materially linked to the monetary instrument or property subject of the freeze order, the covered institution shall freeze these related web of accounts wherever these funds may be found.

The return of the covered institution as required under rule 10.3.c shall include the fact of such freezing and an explanation as to the grounds for the identification of the related web of accounts.

Rule 10.5. Extension of the Freeze Order. - Before the twenty (20) day period of the freeze order issued by the court of appeals expires, the AMLC may apply in the same court for an extension of said period. Upon the timely filing of such application and pending the decision of the Court of Appeals to extend the period, said period shall be deemed suspended and the freeze order shall remain effective.

However, the covered institution shall not lift the effects of the freeze order without securing official confirmation from the AMLC.

Rule 10.6. Prohibition Against Issuance of Freeze Orders Against Candidates for an Electoral Office During Election Period. - No assets shall be frozen to the prejudice of a candidate for an electoral office during an election period.

RULE 11
AUTHORITY TO INQUIRE INTO BANK DEPOSITS

Rule 11.1. Authority to Inquire into Bank Deposits with Court Order. - Notwithstanding the provisions of R.A. No. 1405, as amended; R.A. No. 6426, as amended; R.A. No. 8791, and other laws, the AMLC may inquire into or examine any particular deposit or investment with any banking institution or non-bank financial institution and their subsidiaries and affiliates upon order of any competent court in cases of violation of this Act, when it has been established that there is probable cause that the deposits or investments involved are related to an unlawful activity as defined in Section 3 (i) hereof or a money laundering offense under Section 4 hereof; except in cases as provided under Rule 11.2.

Rule 11.2. Authority to Inquire into Bank Deposits Without Court Order. - The AMLC may inquire into or examine deposit and investments with any banking institution or non-bank financial institution and their subsidiaries and affiliates without a Court Order where any of the following unlawful activities are involved:

(a) Kidnapping for ransom under Article 267 of Act No. 3815, otherwise known as the Revised Penal Code, as amended;

(b) Sections 4,5,6, 8, 9, 10. 12, 13, 14, 15 and 16 of R.A. No. 9165, otherwise known as the Comprehensive Dangerous Drugs Act of 2002;

(c) Hijacking and other violations under R.A. No. 6235; destructive arson and murder, as defined under the Revised

Penal Code, as amended, including those perpetrated by terrorists against non-combatant persons and similar targets.

Rule 11.2.a. Procedure For Examination Without A Court Order. - Where any of the unlawful activities enumerated under the immediately preceding Rule 11.2 are involved, and there is probable cause that the deposits or investments with any banking or non-banking financial institution and their subsidiaries and affiliates are in anyway related to these unlawful activities the AMLC shall issue a resolution authorizing the inquiry into or examination of any deposit or investment with such banking or non-banking financial institution and their subsidiaries and affiliates concerned.

Rule 11.2.b. Duty of the banking institution or non- banking institution upon receipt of the AMLC Resolution. - The banking institution or the non-banking financial institution and their subsidiaries and affiliates shall, immediately upon receipt of the AMLC Resolution, allow the AMLC and/or its authorized representative(s) full access to all records pertaining to the deposit or investment account.

Rule 11.3. - BSP Authority to Examine deposits and investments; Additional Exception to the Bank Secrecy Act. - To ensure compliance with this act, the BSP may inquire into or examine any particular deposit or investment with any banking institution or non-bank financial institution and their subsidiaries and affiliates when the examination is made in the course of a periodic or special examination, in accordance with the rules of examination of the BSP.

Rule 11.3.a. BSP Rules of Examination. - The BSP shall promulgate its rules of examination for ensuring compliance by banks and non-bank financial institutions and their subsidiaries and affiliates with the AMLA and these rules.

Any findings of the BSP which may constitute a violation of any provision of this act shall be transmitted to the AMLC for appropriate action.

RULE 12
FORFEITURE PROVISIONS

Rule 12.1. Authority to Institute Civil Forfeiture Proceedings. – The AMLC is authorized under Section 7 (3) of the AMLA to institute civil forfeiture proceedings and all other remedial proceedings through the Office of the Solicitor General.

Rule 12.2. When Civil Forfeiture May be Applied. – When there is a Suspicious Transaction Report or a Covered Transaction Report deemed suspicious after investigation by the AMLC, and the court has, in a petition filed for the purpose, ordered the seizure of any monetary instrument or property, in whole or in part, directly or indirectly, related to said report, the Revised Rules of Court on civil forfeiture shall apply.

Rule 12.3. Claim on Forfeited Assets. - Where the court has issued an order of forfeiture of the monetary instrument or property in a criminal prosecution for any money laundering offense under Section 4 of the AMLA, the offender or any other person claiming an interest therein may apply, by verified petition, for a declaration that the same legitimately belongs to him, and for segregation or exclusion of the monetary instrument or property corresponding thereto. The verified petition shall be filed with the court which rendered the judgment of conviction and order of forfeiture within fifteen (15) days from the date of the order of forfeiture, in default of which the said order shall become final and

executory. This provision shall apply in both civil and criminal forfeiture.

Rule 12.4. Payment in Lieu of Forfeiture. - Where the court has issued an order of forfeiture of the monetary instrument or property subject of a money laundering offense under Section 4 of the AMLA, and said order cannot be enforced because any particular monetary instrument or property cannot, with due diligence, be located, or it has been substantially altered, destroyed, diminished in value or otherwise rendered worthless by any act or omission, directly or indirectly, attributable to the offender, or it has been concealed, removed, converted or otherwise transferred to prevent the same from being found or to avoid forfeiture thereof, or it is located outside the Philippines or has been placed or brought outside the jurisdiction of the court, or it has been commingled with other monetary instruments or property belonging to either the offender himself or a third person or entity, thereby rendering the same difficult to identify or be segregated for purposes of forfeiture, the court may, instead of enforcing the order of forfeiture of the monetary instrument or property or part thereof or interest therein, accordingly order the convicted offender to pay an amount equal to the value of said monetary instrument or property. This provision shall apply in both civil and criminal forfeiture.

RULE 13
MUTUAL ASSISTANCE AMONG STATES

Rule 13.1. Request for Assistance from a Foreign State. - Where a foreign state makes a request for assistance in the investigation or prosecution of a money laundering offense, the AMLC may execute the request or refuse to execute the same and inform the foreign state of any valid reason for not executing the request or for delaying the execution thereof. The principles of mutuality and reciprocity shall, for this purpose, be at all times recognized.

Rule 13.2. Powers of the AMLC to Act on a Request for Assistance from a Foreign State. - The AMLC may execute a request for assistance from a foreign state by: (1) tracking down, freezing, restraining and seizing assets alleged to be proceeds of any unlawful activity under the procedures laid down in the AMLA and in these Rules; (2) giving information needed by the foreign state within the procedures laid down in the AMLA and in these Rules; and (3) applying for an order of forfeiture of any monetary instrument or property in the court: *Provided,* That the court shall not issue such an order unless the application is accompanied by an authenticated copy of the order of a court in the requesting state ordering the forfeiture of said monetary instrument or property of a person who has been convicted of a money laundering offense in the requesting state, and a certification or an affidavit of a competent officer of the requesting state stating that the conviction and the order of forfeiture are final and that no further appeal lies in respect of either.

Rule 13.3. Obtaining Assistance from Foreign States. - The AMLC may make a request to any foreign state for assistance in (1) tracking down, freezing, restraining and seizing assets alleged to be proceeds of any unlawful activity; (2) obtaining information that it needs relating to any covered transaction, money laundering offense or any other matter directly or indirectly related thereto; (3) to the extent allowed by the law of the foreign state, applying with the proper court therein for an order to enter any premises belonging to or in the possession or control of, any or all of the persons named in said request,

and/or search any or all such persons named therein and/or remove any document, material or object named in said request: *Provided,* That the documents accompanying the request in support of the application have been duly authenticated in accordance with the applicable law or regulation of the foreign state; and (4) applying for an order of forfeiture of any monetary instrument or property in the proper court in the foreign state: *Provided,* That the request is accompanied by an authenticated copy of the order of the Regional Trial Court ordering the forfeiture of said monetary instrument or property of a convicted offender and an affidavit of the clerk of court stating that the conviction and the order of forfeiture are final and that no further appeal lies in respect of either.

Rule 13.4. Limitations on Requests for Mutual Assistance. - The AMLC may refuse to comply with any request for assistance where the action sought by the request contravenes any provision of the Constitution or the execution of a request is likely to prejudice the national interest of the Philippines, unless there is a treaty between the Philippines and the requesting state relating to the provision of assistance in relation to money laundering offenses.

Rule 13.5. Requirements for Requests for Mutual Assistance from Foreign States. - A request for mutual assistance from a foreign state must (1) confirm that an investigation or prosecution is being conducted in respect of a money launderer named therein or that he has been convicted of any money laundering offense; (2) state the grounds on which any person is being investigated or prosecuted for money laundering or the details of his conviction; (3) give sufficient particulars as to the identity of said person; (4) give particulars sufficient to identify any covered institution believed to have any information, document, material or object which may be of assistance to the investigation or prosecution; (5) ask from the covered institution concerned any information, document, material or object which may be of assistance to the investigation or prosecution; (6) specify the manner in which and to whom said information, document, material or object obtained pursuant to said request, is to be produced; (7) give all the particulars necessary for the issuance by the court in the requested state of the writs, orders or processes needed by the requesting state; and (8) contain such other information as may assist in the execution of the request.

Rule 13.6. Authentication of Documents - For purposes of Section 13 (f) of the AMLA and Section 7 of the AMLA, a document is authenticated if the same is signed or certified by a judge, magistrate or equivalent officer in or of, the requesting state, and authenticated by the oath or affirmation of a witness or sealed with an official or public seal of a minister, secretary of state, or officer in or of, the government of the requesting state, or of the person administering the government or a department of the requesting territory, protectorate or colony. The certificate of authentication may also be made by a secretary of the embassy or legation, consul general, consul, vice consul, consular agent or any officer in the foreign service of the Philippines stationed in the foreign state in which the record is kept, and authenticated by the seal of his office.

Rule 13.7. Suppletory Application of the Revised Rules of Court. –

Rule 13.7.1. For attachment of Philippine properties in the name of persons convicted of any unlawful activity as defined in Section 3 (i) of the AMLA,

execution and satisfaction of final judgments of forfeiture, application for examination of witnesses, procuring search warrants, production of bank documents and other materials and all other actions not specified in the AMLA and these Rules, and assistance for any of the aforementioned actions, which is subject of a request by a foreign state, resort may be had to the proceedings pertinent thereto under the Revised Rules of Court.

Rule 13.7.2. Authority to Assist the United Nations and other International Organizations and Foreign States. – The AMLC is authorized under Section 7 (8) and 13 (b) and (d) of the AMLA to receive and take action in respect of any request of foreign states for assistance in their own anti-money laundering operations. It is also authorized under Section 7 (7) of the AMLA to cooperate with the National Government and/or take appropriate action in respect of conventions, resolutions and other directives of the United Nations (UN), the UN Security Council, and other international organizations of which the Philippines is a member. However, the AMLC may refuse to comply with any such request, convention, resolution or directive where the action sought therein contravenes the provision of the Constitution or the execution thereof is likely to prejudice the national interest of the Philippines.

Rule 13.8. Extradition. – The Philippines shall negotiate for the inclusion of money laundering offenses as defined under Section 4 of the AMLA among the extraditable offenses in all future treaties. With respect, however, to the state parties that are signatories to the United Nations Convention Against Transnational Organized Crime that was ratified by the Philippine Senate on 22 October 2001, money laundering is deemed to be included as an extraditable offense in any extradition treaty existing between said state parties, and the Philippines shall include money laundering as an extraditable offense in every extradition treaty that may be concluded between the Philippines and any of said state parties in the future.

RULE 14
PENAL PROVISIONS

Rule 14.1. Penalties for the Crime of Money Laundering.

Rule 14.1.a. Penalties under Section 4 (a) of the AMLA. - The penalty of imprisonment ranging from seven (7) to fourteen (14) years and a fine of not less than Php3.0 Million but not more than twice the value of the monetary instrument or property involved in the offense, shall be imposed upon a person convicted under Section 4 (a) of the AMLA.

Rule 14.1.b. Penalties under Section 4 (b) of the AMLA. - The penalty of imprisonment from four (4) to seven (7) years and a fine of not less than Php1.5 Million but not more than Php3.0 Million, shall be imposed upon a person convicted under Section 4 (b) of the AMLA.

Rule 14.1.c. Penalties under Section 4 (c) of the AMLA. - The penalty of imprisonment from six (6) months to four (4) years or a fine of not less than Php100,000.00 but not more than Php500,000.00, or both, shall be imposed on a person convicted under Section 4(c) of the AMLA.

Rule 14.1.d. Administrative Sanctions. - (1) After due notice and hearing, the AMLC shall, at its discretion, impose fines upon any covered institution, its officers and employees, or any person who violates any of the provisions of R.A. No. 9160, as amended by

R.A. No. 9194 and rules, regulations, orders and resolutions issued pursuant thereto. The fines shall be in amounts as may be determined by the council, taking into consideration all the attendant circumstances, such as the nature and gravity of the violation or irregularity, but in no case shall such fines be less than Php100,000.00 but not to exceed Php500,000.00. The imposition of the administrative sanctions shall be without prejudice to the filing of criminal charges against the persons responsible for the violations.

Rule 14.2. Penalties for Failure to Keep Records - The penalty of imprisonment from six (6) months to one (1) year or a fine of not less than Php100,000.00 but not more than Php500,000.00, or both, shall be imposed on a person convicted under Section 9 (b) of the AMLA.

Rule 14.3. Penalties for Malicious Reporting. - Any person who, with malice, or in bad faith, reports or files a completely unwarranted or false information relative to money laundering transaction against any person shall be subject to a penalty of six (6) months to four (4) years imprisonment and a fine of not less than Php100,000.00 but not more than Php500,000.00, at the discretion of the court: *Provided,* That the offender is not entitled to avail the benefits of the Probation Law.

Rule 14.4. Where Offender is a Juridical Person. - If the offender is a corporation, association, partnership or any juridical person, the penalty shall be imposed upon the responsible officers, as the case may be, who participated in, or allowed by their gross negligence the commission of the crime. If the offender is a juridical person, the court may suspend or revoke its license. If the offender is an alien, he shall, in addition to the penalties herein prescribed, be deported without further proceedings after serving the penalties herein prescribed. If the offender is a public official or employee, he shall, in addition to the penalties prescribed herein, suffer perpetual or temporary absolute disqualification from office, as the case may be.

Rule 14.5. Refusal by a Public Official or Employee to Testify. - Any public official or employee who is called upon to testify and refuses to do the same or purposely fails to testify shall suffer the same penalties prescribed herein.

Rule 14.6. Penalties for Breach of Confidentiality. – The punishment of imprisonment ranging from three (3) to eight (8) years and a fine of not less than Php500,000.00 but not more than Php1.0 Million, shall be imposed on a person convicted for a violation under Section 9(c). In case of a breach of confidentiality that is published or reported by media, the responsible reporter, writer, president, publisher, manager and editor-in-chief shall be liable under this act.

RULE 15
PROHIBITIONS AGAINST POLITICAL HARASSMENT

Rule 15.1. Prohibition against Political Persecution. - The AMLA and these Rules shall not be used for political persecution or harassment or as an instrument to hamper competition in trade and commerce. No case for money laundering may be filed to the prejudice of a candidate for an electoral office during an election period.

Rule 15.2. Provisional Remedies Application; Exception. –

Rule 15.2.a. - The AMLC may apply, in the course of the criminal proceedings, for provisional remedies to prevent the

monetary instrument or property subject thereof from being removed, concealed, converted, commingled with other property or otherwise to prevent its being found or taken by the applicant or otherwise placed or taken beyond the jurisdiction of the court. However, no assets shall be attached to the prejudice of a candidate for an electoral office during an election period.

Rule 15.2.b. - Where there is conviction for money laundering under Section 4 of the AMLA, the court shall issue a judgment of forfeiture in favor of the Government of the Philippines with respect to the monetary instrument or property found to be proceeds of one or more unlawful activities. However, no assets shall be forfeited to the prejudice of a candidate for an electoral office during an election period.

RULE 16
RESTITUTION

Rule 16. Restitution. - Restitution for any aggrieved party shall be governed by the provisions of the New Civil Code.

RULE 17
IMPLEMENTING RULES AND REGULATIONS AND MONEY LAUNDERING PREVENTION PROGRAMS

Rule 17.1. Implementing Rules and Regulations. –

(a) Within thirty (30) days from the effectivity of R.A. No. 9160, as amended by R.A. No. 9194, the BSP, the Insurance Commission and the Securities and Exchange Commission shall promulgate the Implementing Rules and Regulations of the AMLA, which shall be submitted to the Congressional Oversight Committee for approval.

(b) The Supervising Authorities, the BSP, the SEC and the IC shall, under their own respective charters and regulatory authority, issue their Guidelines and Circulars on anti-money laundering to effectively implement the provisions of R.A. No. 9160, as amended by R.A. No. 9194.

Rule 17.2. Money Laundering Prevention Programs. –

Rule 17.2.a. Covered institutions shall formulate their respective money laundering prevention programs in accordance with Section 9 and other pertinent provisions of the AMLA and these Rules, including, but not limited to, information dissemination on money laundering activities and their prevention, detection and reporting, and the training of responsible officers and personnel of covered institutions, subject to such guidelines as may be prescribed by their respective supervising authority. Every covered institution shall submit its own money laundering program to the supervising authority concerned within the non-extendible period that the supervising authority has imposed in the exercise of its regulatory powers under its own charter.

Rule 17.2.b. Every money laundering program shall establish detailed procedures implementing a comprehensive, institution-wide "know-your-client" policy, set-up an effective dissemination of information on money laundering activities and their prevention, detection and reporting, adopt internal policies, procedures and controls, designate compliance officers at management level, institute adequate screening and recruitment procedures, and set-up an audit function to test the system.

Rule 17.2.c. Covered institutions shall adopt, as part of their money laundering programs, a system of flagging and monitoring transactions that qualify as suspicious transactions, regardless of amount or covered

transactions involving amounts below the threshold to facilitate the process of aggregating them for purposes of future reporting of such transactions to the AMLC when their aggregated amounts breach the threshold. All covered institutions, including banks insofar as non-deposit and non-government bond investment transactions are concerned, shall incorporate in their money laundering programs the provisions of these Rules and such other guidelines for reporting to the AMLC of all transactions that engender the reasonable belief that a money laundering offense is about to be, is being, or has been committed.

Rule 17.3. Training of Personnel. - Covered institutions shall provide all their responsible officers and personnel with efficient and effective training and continuing education programs to enable them to fully comply with all their obligations under the AMLA and these Rules.

Rule 17.4. Amendments. - These Rules or any portion thereof may be amended by unanimous vote of the members of the AMLC and submitted to the Congressional Oversight Committee as provided for under Section 19 of R.A. No. 9160, as amended by R.A. No. 9194.

RULE 18
CONGRESSIONAL OVERSIGHT COMMITTEE

Rule 18.1. Composition of Congressional Oversight Committee. - There is hereby created a Congressional Oversight Committee composed of seven (7) members from the Senate and seven (7) members from the House of Representatives. The members from the Senate shall be appointed by the Senate President based on the proportional representation of the parties or coalitions therein with at least two (2) Senators representing the minority. The members from the House of Representatives shall be appointed by the Speaker also based on proportional representation of the parties or coalitions therein with at least two (2) members representing the minority.

Rule 18.2. Powers of the Congressional Oversight Committee. - The Oversight Committee shall have the power to promulgate its own rules, to oversee the implementation of this Act, and to review or revise the implementing rules issued by the Anti-Money Laundering Council within thirty (30) days from the promulgation of the said rules.

RULE 19
APPROPRIATIONS FOR AND BUDGET OF THE AMLC

Rule 19.1. Budget. – The budget of 25 Million Pesos appropriated by Congress under the AMLA shall be used to defray the initial operational expenses of the AMLC. Appropriations for succeeding years shall be included in the General Appropriations Act. The BSP shall advance the funds necessary to defray the capital outlay, maintenance and other operating expenses and personnel services of the AMLC subject to reimbursement from the budget of the AMLC as appropriated under the AMLA and subsequent appropriations.

Rule 19.2. Costs and Expenses. - The budget shall answer for indemnification for legal costs and expenses reasonably incurred for the services of external counsel in connection with any civil, criminal or administrative action, suit or proceedings to which members of the AMLC and the Executive Director and other members of the Secretariat may be made a party by reason of the performance of their functions or duties. The costs and expenses incurred in defending the aforementioned action, suit or proceeding may be paid by the AMLC in advance of the

final disposition of such action, suit or proceeding upon receipt of an undertaking by or on behalf of the member to repay the amount advanced should it be ultimately determined that said member is not entitled to such indemnification.

RULE 20
SEPARABILITY CLAUSE

Rule 20. Separability Clause. – If any provision of these Rules or the application thereof to any person or circumstance is held to be invalid, the other provisions of these Rules, and the application of such provision or Rule to other persons or circumstances, shall not be affected thereby.

RULE 21
REPEALING CLAUSE

Rule 21. Repealing Clause. – All laws, decrees, executive orders, rules and regulations or parts thereof, including the relevant provisions of R.A. No. 1405, as amended; R.A. No. 6426, as amended; R.A. No. 8791, as amended, and other similar laws, as are inconsistent with the AMLA, are hereby repealed, amended or modified accordingly.

RULE 22
EFFECTIVITY OF THE RULES

Rule 22. Effectivity. – These Rules shall take effect after its approval by the Congressional Oversight Committee and fifteen (15) days after its complete publication in the Official Gazette or in a newspaper of general circulation.

RULE 23
TRANSITORY PROVISIONS

Rule 23.1. - Transitory Provisions. - Existing freeze orders issued by the AMLC shall remain in force for a period of thirty (30) days after effectivity of this act, unless extended by the Court of Appeals.

Rule 23.2. - Effect of R.A. No. 9194 on Cases for Extension of Freeze Orders Resolved by the Court of Appeals. - All existing freeze orders which the Court of Appeals has extended shall remain effective, unless otherwise dissolved by the same court.

INVESTMENT HOUSES AND FINANCING COMPANIES (IH/FC) WITH QUASI-BANKING FUNCTIONS

[Appendix to Subsec. 4601Q.2 (2008 - 4602Q.1)]

(Deleted by Circular No. 636 dated 17 December 2008)

DETAILS ON THE COMPUTATION OF QUARTERLY INTEREST PAYMENTS CREDITED TO THE DEMAND DEPOSIT ACCOUNTS OF QUASI-BANKS' LEGAL RESERVE DEPOSITS WITH THE BANGKO SENTRAL

[Appendix to Subsec. 4254Q.3 (2008 - 4246Q.7)]

The following are the pertinent information on the computation of quarterly interest payments credited to the DDAs of QBs' legal reserve deposits with BSP.

1. BSP Circular No. 262, as amended, (for regular DDA) and Memorandum to All Banks and Other Financial Intermediaries Performing Trust, Other Fiduciary Business and Investment Management Activities (for CTF and TOFA), as amended, both dated 18 October 2000 state that computation of quarterly interest payments due on QBs' legal reserve deposits with the BSP is based on the lower of their outstanding daily DDA balance and forty percent (40%) of the reserve requirement (excluding liquidity reserve). Interest rate is at four percent (4%) per annum and interest base at 365 days.

2. The daily DDA balance used in the computation of interest may be obtained from the semi-monthly demand deposit statements of account balances that are available electronically to QBs through EFTIS (for *PhilPaSS* participants) or monthly through the DDA statements sent by mail (for non-*PhilPaSS* participants).

3. The data on reserve requirements are based on the institutions' Consolidated Report of Condition Required and Available Reserves against deposit substitutes and special financing submitted to the SDC on a weekly basis. Unless SDC furnishes an amended data, the QB's computation is used in determining the forty percent (40%) of the reserve requirement that shall be compared with the outstanding daily balance, in arriving at the amount of interest credit.

4. The interest credit to each DDA is supported by a credit advice which indicates the period covered by the payment. For *PhilPaSS* participants, the credit advices are released through their authorized QB representatives together with the cancelled checks drawn against the institutions' DDA with the BSP while for non-*PhilPaSS* participants, the credit advices are sent by mail together with their DDA Statement of Accounts.

TRANSFER/SALE OF NON-PERFORMING ASSETS TO A SPECIAL PURPOSE VEHICLE OR TO AN INDIVIDUAL

[Appendix to Sec. 4394Q.10 (2008 - 4396Q)]

The following procedures shall govern the transfer/sale of NPAs to a SPV or to an individual that involves a single family residential unit, or transactions involving *dacion en pago* by the borrower or third party of a NPL, for the purpose of obtaining the COE which is required to avail of the incentives provided under R.A. No. 9182, as amended by R.A. No. 9343.

a. Prior to the filing of any application for transfer/sale of NPAs, a QB shall coordinate with the BSP through the SDC and the appropriate department of the SES to develop a reconciled and finalized master list of its eligible NPAs.

For this purpose, QBs were requested to submit a complete inventory of their NPAs in the format prescribed under Circular Letter dated 07 January 2003. Only NPAs included in the masterlist that meet the definition of NPA, NPL and ROPA under R.A. No. 9182 may qualify for the COE. The QBs shall be provided a copy of their reconciled and finalized masterlist for their guidance.

Only QBs which have not yet submitted their masterlist of NPAs and intend to avail of the incentives and fee privileges of the SPV Act 2nd Phase implementation are allowed to submit a complete inventory of their NPAs in the format prescribed under Circular Letter dated 07 January 2003. QBs which have already submitted to BSP a masterlist of NPAs as of 30 June 2002 in the 1st Phase implementation of the SPV Act will not be allowed to submit a new/amended masterlist.

b. An application for eligibility of specific NPAs shall be filed in writing (hard copy) by the selling QB with the BSP through the appropriate department of the SES for each proposed transfer of asset/s. Although no specific form is prescribed, the applicant shall describe in sufficient detail its proposed transaction, identifying its counterparty/ies and disclosing the terms, conditions and all material commitments related to the transaction.

c. For applications involving more than ten (10) NPA accounts, the list of NPAs to be transferred/sold shall be submitted in soft copy (by electronic mail or diskette) in excel format using the prescribed data structure/format for NPLs and ROPAs to the appropriate department of the SES of the applicant QB at the following addresses:

SEDI-SPV@bsp.gov.ph
SEDII-SPV@bsp.gov.ph
SEDIII-SPV@bsp.gov.ph
SEDIV-SPV@bsp.gov.ph

For applications involving ten (10) NPA accounts or less, it is preferable that the list be submitted also in soft copy. The applicant may opt to submit the list in hard copy, provided all the necessary information shown in the prescribed data structure that are relevant to each NPL or ROPA to be transferred/sold will be indicated. The list to be submitted in hard copy would be ideal for the sale/transfer of NPAs that involve one (1) promissory note and/or one (1) asset item per account.

d. The application shall be accompanied by a written certification signed by a senior officer with a rank of at least senior vice president or equivalent, who is authorized by the board of directors, or by the country head, in the case of foreign banks, that:

(1) the assets to be sold/transferred are NPAs as defined under the SPV Act of 2002;

(2) the proposed sale/transfer of said NPAs is under a true sale;

(3) the notification requirement to the borrowers has been complied with; and

(4) the maximum ninety (90)-day period for renegotiation and restructuring has been complied with.

Items *(3)* and *(4)* above shall not apply if the NPL has become a ROPA after 30 June 2002.

e. In the case of *dacion en pago* by the borrower or a third party to a QB, the application for COE on the NPL being settled shall be accompanied by a Deed of Dacion executed by the borrower, the third party, the registered owner of the property and the QB.

f. The appropriate department of the SES may conduct an on-site review of the NPLs and ROPAs proposed to be transferred/sold. After the on-site review, the application for transfer/sale shall be submitted to the Deputy Governor, SES for approval and for the issuance of the corresponding COE.

g. Upon the issuance of the SPV Application Number by the BSP, a QB shall be charged a processing fee, as follows:

(1) 1/100 of one percent (1%) of the book value of NPAs transferred or the transfer price, whichever is higher, but not below ₱25,000 if the transfer is made to an SPV;

(2) 1/100 of 1% of the book value of the NPL but not below ₱5,000 in case of a *dacion en pago* arrangement by an individual or corporate borrower;

(3) ₱5,000 if the transfer involves a single family residential unit to an individual.

h. An SPV that intends to transfer/sell to a third party an NPA that is covered by a COE previously issued by the BSP shall file an application for such transfer/sale with the SEC which shall issue the corresponding COE based on the data base of COEs maintained at the BSP.

An individual who intends to transfer/sell an NPA that involves a single family residential unit he had acquired that is covered by a COE shall file an application for the another COE with the BSP through the QB from which the NPA was acquired. The individual shall indicate in his application the previous COE issued for the NPA he had acquired and the name, address and TIN of the transferee/buyer of the NPA. A processing fee of ₱5,000 shall be collected by BSP upon issuance of the SPV Application Number by the BSP.

(As amended by M-2006-001 dated 11 May 2006)

ACCOUNTING GUIDELINES ON THE SALE OF NON-PERFORMING ASSETS TO SPECIAL PURPOSE VEHICLES AND TO QUALIFIED INDIVIDUALS FOR HOUSING UNDER "THE SPECIAL PURPOSE VEHICLE ACT OF 2002"

[Appendix to Sec. 4394Q.10 (2008 - 4396Q)]

General Principles

These guidelines set out alternative regulatory accounting treatment of the sale of NPAs by banks and other FIs under BSP supervision to SPVs and to qualified individuals for housing under R.A. No. 9182, otherwise known as "The Special Purpose Vehicle Act of 2002".

The guidelines recognize that banks/FIs may need temporary regulatory relief, in addition to tax relief under the SPV Law, particularly in the timing of recognition of losses, so that they may be encouraged to maximize the sale of their NPAs even at substantial discounts: *Provided, however*, That in the interest of upholding full transparency and sustaining market discipline, banks/FIs that avail of such regulatory relief shall fully disclose its impact in all relevant financial reports.

The guidelines cover the following areas:

(1) Derecognition of NPAs sold/transferred to an SPV and initial recognition of financial instruments issued by the SPV to the selling bank/FI as partial or full settlement of the NPAs sold/transferred to the SPV;

(2) Subsequent measurement of the carrying amount of financial instruments issued by the SPV to the selling bank/FI;

(3) Capital adequacy ratio (CAR) calculation; and

(4) Disclosure requirement on the selling bank/FI.

The sale/transfer of NPAs to SPV referred to in these guidelines shall be in the nature of a "true sale" pursuant to Section 13 of the SPV Law and its Implementing Rules and Regulations.

I. Derecognition of NPAs Sold and Initial Recognition of Financial Instruments Received

A bank/FI should derecognize an NPA in accordance with the provisions of PAS 39 (for financial assets such as loans and securities) and PAS 16 and 40 (for non-financial assets such as land, building and equipment).

A sale of NPA qualifying as a true sale pursuant to Section 13 of the SPV Law and its Implementing Rules and Regulations but not qualifying for derecognition under PASs 39, 16 and 40 may nonetheless, be derecognized. *Provided:* That the bank/FI shall disclose such fact, in addition to all other disclosures provided in this Appendix.

On derecognition, any excess of the carrying amount of the NPA (i.e., net of specific allowance for probable losses after booking the BSP recommended valuation reserve) over the proceeds received in the form of cash and/or financial instruments issued by the SPV represents an actual loss that should be charged to current period's operations.

However, a bank/FI may use any existing specific allowance for probable losses on NPA sold:

(1) to cover any unbooked (specific/general) allowance for probable losses; and

(2) to apply the excess, if any, as additional (specific/general) allowance for probable losses, on remaining assets, in which case the carrying amount of the NPA

(which is compared with the proceeds received for purposes of determining the actual loss) shall be the gross amount of the NPA: *Provided,* That the use of such existing specific allowance for probable losses on the NPA sold as provisions against remaining assets shall be properly disclosed.

The loss may, moreover, be booked under "Deferred Charges" account which should be written down over the next ten (10) years based on the following schedule:

End of Period From Date of Transaction	Cumulative Write-down of Deferred Charges
Year 1	5%
Year 2	10%
Year 3	15%
Year 4	25%
Year 5	35%
Year 6	45%
Year 7	55%
Year 8	70%
Year 9	85%
Year 10	100%

Provided, That the staggered booking of actual loss on sale/transfer of the NPA shall be properly disclosed.

In case the face amounts of the financial instruments exceed the excess of the carrying amount of the NPA over the cash proceeds, the same shall be adjusted by setting up specific allowance for probable losses so that no gain shall be recognized from the transaction.

The carrying amount of the NPA shall be initially assumed to be the NPA's fair value. The excess of the carrying amount of the NPA over the cash proceeds or the face amounts of the financial instruments, whichever is lower, shall then be the initial cost of financial instruments received.

Banks/FIs shall book such financial instruments under the general ledger account "Unquoted Debt Securities Classified as Loans" for debt instruments or "Investments in Non-Marketable Equity Securities" for equity instruments.

Consolidation of SPV with Bank/FI. Even if the sale of NPAs to SPVs qualifies for derecognition, a bank/FI shall consolidate the SPV in the audited consolidated financial statements when the relationship between the bank/FI and the SPV indicates that the SPV is controlled by the bank/FI in accordance with the provisions of SIC (Standing Interpretations Committee) -12 Consolidation - Special Purpose Entities.

II. Subsequent Measurement of Financial Instruments Received

(a) A bank/FI should assess at end of each fiscal year or more frequently whether there is any objective evidence or indication based on analysis of expected net cash inflows that the carrying amount of financial instruments issued by an SPV may be impaired. A financial instrument is impaired if its carrying amount (i.e., net of specific allowance for probable loss) is greater than its estimated recoverable amount. The estimated recoverable amount is determined based on the net present value of expected future cash flows discounted at the current market rate of interest for a similar financial instrument.

In applying discounted cash flow analysis, a bank/FI should use the discount rate(s) equal to the prevailing rate of return for financial instruments having substantially the same terms and characteristics, including the creditworthiness of the issuer.

(b) Alternatively, the estimated recoverable amount of the financial instruments may be determined based on an updated estimate of residual NPV of the issuing SPV.

The estimated recoverable amount of the financial instrument shall be the present value of the excess of expected cash inflows (e.g., proceeds from the sale of collaterals and/or ROPAs, which in no case shall exceed the contract price of the NPAs sold/ transferred, interest on the reinvestment of proceeds) over expected cash outflows (e.g., direct costs to sell, administrative expenses, principal and interest payments on senior obligations, interest payments on the financial instruments).

The fair market value of the collateral and/or ROPAs should under this method be considered only under the following conditions:

(1) The appraisal was performed by an independent appraiser acceptable to the BSP; and

(2) The valuation of the independent appraiser is based on current market valuation of similar assets in the same locality as underlying collateral rather than other valuation methods such as replacement cost, etc.

The assumptions regarding the timing of sale, the direct cost to sell, administrative expenses, reinvestments rate and current market rate should be disclosed in sufficient detail in the audited financial statements. The applicable discount rate should be based on the implied stripped yield of the Treasury note or bond for the tenor plus an appropriate risk premium.

(c) In case of impairment, the carrying amount of the financial instrument should be reduced to its estimated recoverable amount, through the use of specific allowance for probable losses account that should be charged to current period's operations. However, at the end of the fiscal year the sale/transfer of NPA occurred, such setting up of specific allowance for probable losses account may be booked on a staggered basis over the next ten (10) years based on the following schedule:

End of Period From Date of Transaction	Cumulative Booking of Allowance for Probable Losses
Year 1	5%
Year 2	10%
Year 3	15%
Year 4	25%
Year 5	35%
Year 6	45%
Year 7	55%
Year 8	70%
Year 9	85%
Year 10	100%

Provided, That the staggered booking of impairment, if any, upon remeasurement of financial instruments at end of the fiscal year the sale/transfer of the NPA occurred shall be properly disclosed.

After initially recognizing an impairment loss, the bank/FI should review the financial instruments for future impairment in subsequent financial reporting date.

If in a subsequent period, the estimated recoverable amount of the financial instrument decreases, the bank/FI should immediately book additional allowance for probable losses corresponding to the decrease. However, a bank/FI may stagger the booking of such additional allowance for probable losses in such a way that it catches up and keeps pace with the original deferral schedule (e.g., if the impairment occurred in Year 8, a bank/FI should immediately book 70 percent (70%) at end of Year 8, and thereafter, additional 15 percent (15%) each at end of Year 9 and Year 10, respectively): *Provided,* That the staggered booking of impairment, if any, upon remeasurement of financial instruments shall be properly disclosed.

If in a subsequent period, the estimated recoverable amount of the financial instrument increases exceeding its carrying amount, and the increase can

be objectively related to an event occurring after the write-down, the write-down of the financial instruments should be reversed by adjusting the specific allowance for probable losses account. The reversal should not result in a carrying amount of the financial instrument that exceeds what the cost would have been had the impairment not been recognized at the date the write-down of the financial instrument is reversed. The amount of the reversal should be included in the profit for the period.

Illustrative accounting entries for derecognition of NPAs, initial recognition of financial instruments issued by the SPV, and subsequent measurement of the carrying amount of the financial instrument are in Annex Q-28-a-1.

III. CAR Calculation

Banks/FIs may, for purposes of calculating CAR, likewise stagger over a period of seven (7) years the recognition of:

(1) actual loss on sale/transfer of NPAs; and

(2)impairment, if any, upon remeasurement of financial instruments, in accordance with the following schedule:

End of Period From Date of Transaction	Cumulative Recognition of Losses/Impairment
Year 1	5%
Year 2	10%
Year 3	15%
Year 4	25%
Year 5	35%
Year 6	45%
Year 7	55%
Year 8	70%
Year 9	85%
Year 10	100%

Provided, That no cash dividend on common stock and/or preferred stock shall be declared by the bank/FI while the staggered recognition of actual loss on sale/transfer of NPA and/or impairment, if any, on the remeasurement of financial instruments at end of the first fiscal year following the sale/transfer of NPA exist.

The financial instruments received by the selling bank/FI shall be risk weighted in accordance with Sec. 4115Q.

A bank/FI may declare cash dividend on common and/or preferred stock notwithstanding deferred recognition of loss duly authorized by the BSP.

IV. Disclosure

Banks/FIs should disclose as "Additional Information" in periodic reports submitted to the BSP, as well as in published reports and audited financial statements and all relevant financial reports the specific allowance for probable losses on NPAs sold used as provisions against remaining assets, the staggered recognition of actual loss on sale/transfer of NPAs" and/or impairment, if any, on the remeasurement of financial instruments.

In addition, banks/FIs which receive financial instruments issued by the SPVs as partial or full settlement of the NPAs transferred to the SPVs should disclose in the AFS the method used and the significant assumptions applied in estimating the recoverable amount of the financial instruments, including the timing of the sale, the direct cost to sell, administrative expenses, reinvestment rate, current market rate, etc. (The pro-forma disclosure requirements on the staggered recognition of actual loss on sale/transfer of NPAs and/or impairment, if any, on the remeasurement of financial instruments are shown in Annex Q-28-a-2.)

Annex Q-28-a-1

ILLUSTRATIVE ACCOUNTING ENTRIES TO RECORD SALE OF NPAs TO SPV UNDER THE SPV LAW OF 2002 UNDER DEFERRED RECOGNITION OF LOSS/IMPAIRMENT OF FINANCIAL INSTRUMENTS

	Mode of Payment (Cash, Financial Instruments)				
	Cash Only (30, 0)	Financial Instruments Only (0, 120)	Part Cash, Part Financial Instruments [1] (30,100)	Part Cash, Part Financial Instruments[2] (30, 90)	Part Cash, Part Financial Instruments (30, 70)
Assumptions:					
Loans/ROPAs, gross	120	120	120	120	120
Allowance for probable losses	20	20	20	20	20
Loans/ROPAs, net	100	100	100	100	100
Cash payment received	30	0	30	30	30
Financial instruments received	0	120	100	90	70
Unbooked valuation reserves on remaining assets	15	15	15	15	15

[1] Face amounts of financial instruments exceed the excess of the gross amount of the NPAs over the cash proceeds.

[2] Face amounts of financial instruments do not exceed the excess of the gross amount of the NPAs over the cash proceeds.

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	Accounting Entries	Cash Only (30, 0)		Financial Instruments Only (0, 120)		Part Cash, Part Financial Instruments [1] (30, 100)		Part Cash, Part Financial Instruments [2] (30, 90)		Part Cash, Part Financial Instruments (30, 70)	
		Debit	Credit	Debit	Credit	Debit	Credit	Debit	Credit	Debit	Credit
1	Allowance for Probable Losses – NPAs sold Allowance For Probable Losses - Remaining Assets *(For unbooked provisions)* *(As additional provisions)* To record the reclassification of existing specific allowance for credit losses on NPAs sold as provisions against remaining assets.	20	 15 5	20	 15 5	20	 15 5	20	 15 5	20	 15 5
2	Cash Unquoted Debt Securities Classified as Loans/INMES Deferred Charges Loans/ROPAs Allowance for Credit Losses - Unquoted Debt Securities Classified as Loans/INMES To record the sale of NPAs, receipt of cash and/or financial instruments, and deferred recognition of loss, if any.	30 0 90	 120 0	0 120 0	 120 0	30 100 0	 120 10	30 90 0	 120 0	30 70 20	 120 0
3	Amortization – Deferred Charges Deferred Charges To record annual write down of deferred charges based on schedule of staggered booking of losses.	xxx	xxx	0	0	0	0	0	0	xxx	xxx
4	Provision for Credit Losses – Unquoted Debt Securitues Classified as Loans/INMES Allowance for Credit Losses – Unquoted Debt Securities Classified as Loans/INMES To record annual build up of allowance for credit losses on financial instruments based on schedule of staggered booking of allowance for credit losses.	0	 0	xxx	 xxx	xxx	 xxx	xxx	 xxx	xxx	

[1] Face amounts of financial instruments exceed the excess of the gross amount of the NPAs over the cash proceeds.
[2] Face amounts of financial instruments do not exceed the excess of the gross amount of the NPAs over the cash proceeds.

Annex Q-28-a-2

PRO-FORMA DISCLOSURE REQUIREMENT

A. Statement of Condition

Particulars	Amount		
	Qualified for derecognition Under PFRS/PAS	Not Qualified for derecognition Under PFRS/PAS	Total
Additional Information:			
NPAs sold, gross	xxx	xxx	xxx
Allowance for credit losses (specific) on NPAs sold	xxx	xxx	xxx
Allowance for credit losses (specific) on NPAs sold applied to:			
Unbooked allowance for credit losses:			
Specific	xxx	xxx	xxx
General	xxx	xxx	xxx
Additional allowance for credit losses			
Specific	xxx	xxx	xxx
General	xxx	xxx	xxx
Cash received	xxx	xxx	xxx
Financial instruments received, gross	xxx	xxx	xxx
Less: Allowance for credit losses (specific)	xxx	xxx	xxx
Carrying amount of financial instruments received	xxx	xxx	xxx
Less: Unbooked allowance for credit losses (specific)	xxx	xxx	xxx
Adj. carrying amount of financial instruments received	xxx	xxx	xxx
Deferred charges, gross	xxx	xxx	xxx
Less: Deferred charges written down	xxx	xxx	xxx
Carrying amount of deferred charges	xxx	xxx	xxx

B. Statement of Income and Expenses

Particulars	Amount		
	Qualified for derecognition Under PFRS/PAS	Not Qualified for derecognition Under PFRS/PAS	Total
Additional Information:			
Net income/(loss) after income tax *(with regulatory relief)*			xxx
Less: Deferred charges not yet written down	xxx	xxx	xxx
Unbooked allowance for credit losses (specific) on financial instruments received	xxx	xxx	xxx
Total deduction	xxx	xxx	xxx
less: Deferred tax liability, if applicable	xxx	xxx	xxx
Net deductions	xxx	xxx	xxx
Net income/(loss) after income tax *(without regulatory relief)*			

SIGNIFICANT TIMELINES RELATIVE TO THE IMPLEMENTATION OF R.A. NO. 9182, ALSO KNOWN AS THE "SPECIAL PURPOSE VEHICLE ACT", AS AMENDED BY R.A. NO. 9343

[Appendix to Sec. 4394Q.10 (2008 - 4396Q]

A. Filing of Applications with the SEC for Establishing an SPV

Under Section 6 of R.A. No. 9182, as amended by R.A. No. 9343, applications for the establishment and registration of an SPV shall be filed with the SEC within eighteen (18) months from the effectivity of the amendatory Act (i.e., up to 14 November 2007).

B. Sale/Transfer of NPAs Entitled to Tax Exemptions and Fee Privileges

The following transactions enumerated as Items *"1"* to *"6"* of Section 15 of the IRR of the SPV Law are entitled to the tax exemptions and fee privileges under the same Section only if such transactions occur within two (2) years from the effectivity of the amendatory Act or from 14 May 2006 to 14 May 2008:[1]

1. The transfer of the NPL by the FI to an SPV;
2. The transfer of the ROPA by the FI to an SPV;
3. The dation in payment *(dacion en pago)* of the NPL by the borrower to the FI;
4. The dation in payment *(dacion en pago)* of the NPL by a third party, on behalf of the borrower, to the FI;
5. The transfer of the NPL (secured by a real estate mortgage on a residential unit) by the FI to an individual; and
6. The transfer of the ROPA (single family residential unit) by the FI to an individual.

For purposes of determining whether a transaction occurred within the two (2)-year period or from 14 May 2006 to 14 May 2008, relevant documents to support the application (e.g., Asset Sale and Purchase Agreement, Deed of Assignment, Deed of Dation, etc.) should be notarized within the said two (2)-year period.

(M-2007 -013 dated 11 May 2007 as amended by M-2008-014 dated 17 March 2008)

[1] The Monetary Board authorized the SES to accept applications for Certificate of Eligibility (COE) until 13 June 2008, or up to 30 days after the 14 May 2008 deadline.

GUIDELINES AND MINIMUM DOCUMENTARY REQUIREMENTS FOR FOREIGN EXCHANGE FORWARD AND SWAP TRANSACTIONS

[Appendix to Subsecs. 4625Q.3 - 4625Q.4 and 4625Q.6 (2008 - 4603Q.16 - 4603Q.18)]

The following is a list of minimum documentary requirements for FX forward and swap transactions. Unless otherwise indicated, original documents[1] shall be presented on or before deal date to QBs.

A. FORWARD SALE OF FX TO COVER OBLIGATIONS – DELIVERABLE AND NON-DELIVERABLE

1. *FORWARD SALE OF FX – TRADE*

1.1 Trade transactions

1.1.1 Under LC

a. Copy of LC opened; and

b. Accepted draft, or commercial invoice/Bill of Lading

1.1.2 Under DA/OA arrangements

a. Certification of reporting QB on the details of DA/OA under Schedule 10 (Import Letters of Credits Opened and DA/OA Import Availments and Extensions) of FX Form 1 (Consolidated Report on Foreign Exchange Assets and Liabilities); and

b. Copy of commercial invoice;

In addition to the above requirements, the QB shall require the customer to submit a Letter of Undertaking that:

(i.) Before or at maturity date of the forward contract, it (the importer) shall comply with the documentation requirements on sale of FX for trade transactions under existing regulations; and

(ii.) No double hedging has been obtained by the customer for the covered transactions.

1.1.3 Direct Remittance

Original shipping documents indicated in Item *"II.a"* of Circular Letter dated 24 January 2002.

2. *NON-TRADE TRANSACTIONS*

Only non-trade transactions with specific due dates shall be eligible for forward contracts, and shall be subject to the same documentation requirements under Circular No. 388 dated 26 May 2003 with the following additional guidelines for foreign currency loans and investments.

2.1 Foreign Currency Loans owed to non-residents or AABs

2.1.1 Deliverable Forwards

The maturing portion of the outstanding eligible obligation, i.e., those that are registered with the BSP registration letter, may be covered by a deliverable forward subject to the documentary requirements under Circular No. 388. A copy of the creditor's billing statement may be submitted only on or before the maturity date of the contract.

2.1.2 NDFs

The outstanding eligible obligation, i.e., those that are registered with the BSP, including interests and fees thereon as indicated in the BSP registration letter may be covered by a NDF, subject to the documentary requirements under Circular No. 388, except for the creditor's billing statement which need not be submitted.

The amount of the forward contract shall not exceed the outstanding amount of the underlying obligation during the term of the contract.

2.2 Inward Foreign Investments

The unremitted amount of sales/ maturity proceeds due for repatriation to non-resident investors pertaining to BSP - registered investments in the following instruments issued by a Philippine resident:

a. shares of stock listed in the PSE;

b. GS;

[1] If copy is indicated, it shall mean photocopy, electronic copy or facsimile of original.

c. money market instruments; and

d. peso time deposits with a minimum tenor of ninety (90) days may be covered by FX forward contracts subject to the presentation of the original BSRD on or before deal date. However, for Item *"2.2.a"* above, original BSRD or BSRD Letter-Advice, together with the broker's sales invoice, shall be presented on or before maturity date of the FX forward contract, which date coincides with the settlement date of the PSE transaction.

Sales proceeds of BSP-registered investments in shares of stock that are not listed in the PSE may be covered by a deliverable FX forward contract only if determined to be outstanding as of the deal date for the contract and payable on a specific future date as may be indicated in the Contract To Sell/Deed of Absolute Sale and subject to the same documentary requirements under Circular No. 388.

B. FORWARD SALE OF FX TO COVER EXPOSURES– DELIVERABLE AND NON-DELIVERABLE

1. *TRADE (DELIVERABLE AND NON-DELIVERABLE)*

1.1 Under LC

a. Copy of LC opened; and

b. Proforma Invoice, or Sales Contract/Purchase Order

1.2 Under DA/OA, Documents Against Payment (DP) or Direct Remittance (DR)

Any of the following where delivery or shipment shall be made not later than one (1) year from deal date:

a. Sales Contract

b. Confirmed Purchase Order

c. Accepted Proforma Invoice

d. Shipment/Import Advice of the Supplier

In addition to the above requirements, the QB shall require the customer to submit a Letter of Undertaking that:

(i) At maturity of the forward contract, it shall comply with the documentation requirements on the sale of FX for trade transactions under Circular-Letter dated 24 January 2002, as amended; and

(ii) No double hedging has been obtained by the customer for the covered transactions.

2. *NON-TRADE (NON-DELIVERABLE)*

The outstanding balance of BSP-registered foreign investments without specific repatriation date, appearing in the covering BSRD may only be covered by an NDF contract, based on its market/book value on deal date, subject to prior BSP approval and if already with BSRD presentation of the covering BSRD and the proof that the investment still exists (e.g., stock certificate, or broker's buy invoice, or confirmation of sale, or certificate of investment in money market instruments, or certificate of peso time deposits). Hedging for permanently assigned capital of Philippine branches of foreign banks/firms is not allowed.

C. FORWARD PURCHASE OF FX

Such FX forward contracts shall be subject to the QB's "Know Your Customer" policy and existing regulations on anti-money laudering. In addition, counterparties must be limited to those that are manifestly eligible to engage in FX forwards as part of the normal course of their operations and which satisfy the QB's suitability and eligibility rules for such transactions.

D. FX SWAP TRANSACTIONS

1. *FX SALE (first leg)/FORWARD FX PURCHASE (second leg)*

The same minimum documentary requirements for sale of FX under BSP

Circular No. 388 for non-trade transactions, and Circular-Letter dated 24 January 2002, as amended, for trade transactions, shall be presented on or before deal date.

2. *FX PURCHASE (first leg)/FORWARD FX SALE (second leg)*

The first leg of the swap will be subject to the QB's "Know Your Customer" policy and existing regulations on anti-money laundering. The second leg of the swap transaction will be subject to the swap contract between the counterparties.

Swap contracts of this type intended to fund peso loans to be extended by non-residents in favor of residents shall require prior BSP approval.

(As amended by Circular No. 591 dated 15 October 2007)

GUIDELINES TO GOVERN THE SELECTION, APPOINTMENT, REPORTING REQUIREMENTS AND DELISTING OF EXTERNAL AUDITORS AND/OR AUDITING FIRM OF COVERED ENTITIES

[Appendix to Sec. 4189Q (2008 - 4180Q) and 4162Q (2008 - 4190Q)]

Pursuant to Section 58 of the Republic Act No. 8791, otherwise known as "The General Banking Law of 2000", and the existing provisions of the executed Memorandum of Agreement (hereinafter referred to as the MOA) dated 12 August 2009, binding the Bangko Sentral ng Pilipinas (BSP), Securities and Exchange Commission (SEC), Professional Regulation Commission (IC) - Board of Accountancy (BOA) and the Insurance Commission (IC) for a simplified and synchronized accreditation requirements for external auditor and/or auditing firm, the Monetary Board, in its Resolution No. 950 dated 02 July 2009, approved the following revised rules and regulations that shall govern the selection and delisting by the BSP of covered institution which under special laws are subject to BSP supervision.

A. STATEMENT OF POLICY

It is the policy of the BSP to ensure effective audit and supervision of banks, QBs, trust entities and/or NSSLAs including their subsidiaries and affiliates engaged in allied activities and other FIs which under special laws are subject to BSP supervision, and to ensure reliance by BSP and the public on the opinion of external auditors and auditing firms by prescribing the rules and regulations that shall govern the selection, appointment, reporting requirements and delisting for external auditors and auditing firms of said institutions, subject to the binding provisions and implementing regulations of the aforesaid MOA.

B. COVERED ENTITIES

The proposed amendment shall apply to the following supervised institution, as categorized below, and their external auditors:

1. *Category A*
   a. UBs/KBs;
   b. Foreign banks and branches or subsidiaries of foreign banks, regardless of unimpaired capital; and
   c. Banks, trust department of qualified banks and other trust entities with additional derivatives authority, pursuant to Sec. X611 regardless of classification, category and capital position.
2. *Category B*
   a. TBs;
   b. QBs;
   c. Trust department of qualified banks and other trust entities;
   d. National Coop Banks; and
   e. NBFIs with quasi-banking functions.
3. *Category C*
   a. RBs;
   b. NSSLAs;
   c. Local Coop Banks; and
   d. Pawnshops.

The above categories include their subsidiaries and affiliates engaged in allied activities and other FIs which are subject to BSP risk-based and consolidated supervision: *Provided,* That an external auditor who has been selected by the BSP to audit entities under *Category B* and *C* and if selected by the BSP to audit covered entities under *Category B* is automatically qualified to audit entities under *Category C*.

C. DEFINITION OF TERMS

The following terms shall be defined as follows:

1. *Audit* – an examination of the financial statements of any issuer by an external auditor in compliance with the rules

of the BSP or the SEC in accordance with then applicable generally accepted auditing and accounting principles and standards, for the purpose of expressing an opinion on such statements.

2. *Non-audit services* – any professional services provided to the covered institution by an external auditor, other than those provided to a covered institution in connection with an audit or a review of the financial statements of said covered institution.

3. *Professional Standards* - includes: (a) accounting principles that are (1) established by the standard setting body; and (2) relevant to audit reports for particular issuers, or dealt with in the quality control system of a particular registered public accounting firm; and (b) auditing standards, standards for attestation engagements, quality control policies and procedures, ethical and competency standards, and independence standards that the BSP or SEC determines (1) relate to the preparation or issuance of audit reports for issuers; and (2) are established or adopted by the BSP or promulgated as SEC rules.

4. *Fraud* – an intentional act by one (1) or more individuals among management, employees, or third parties that results in a misrepresentation of financial statements, which will reduce the consolidated total assets of the company by five percent (5%). It may involve:

a. Manipulation, falsification or alteration of records or documents;

b. Misappropriation of assets;

c. Suppression or omission of the effects of transactions from records or documents;

d. Recording of transactions without substance;

e. Intentional misapplication of accounting policies; or

f. Omission of material information.

5. *Error* - an intentional mistake in financial statements, which will reduce the consolidated total assets of the company by five percent (5%). It may involve:

a. Mathematical or clerical mistakes in the underlying records and accounting data;

b. Oversight or misinterpretation of facts; or

c. Unintentional misapplication of accounting policies.

6. *Gross negligence* - wanton or reckless disregard of the duty of due care in complying with generally accepted auditing standards.

7. *Material fact/information* - any fact/information that could result in a change in the market price or value of any of the issuer's securities, or would potentially affect the investment decision of an investor.

8. *Subsidiary* - a corporation or firm more than fifty percent (50%) of the outstanding voting stock of which is directly or indirectly owned, controlled or held with power to vote by a bank, QB, trust entity or NSSLA.

9. *Affiliate* - a corporation, not more than fifty percent (50%) but not less than ten percent (10%) of the outstanding voting stock of which is directly or indirectly owned, controlled or held with power to vote by a bank, QB, trust entity or NSSLA and a juridical person that is under common control with the bank, QB, trust entity or NSSLA.

10. *Control* - exists when the parent owns directly or indirectly more than one half of the voting power of an enterprise unless, in exceptional circumstance, it can be clearly demonstrated that such ownership does not constitute control.

Control may also exist even when ownership is one half or less of the voting power of an enterprise when there is:

a. Power over more than one half of the voting rights by virtue of an agreement with other stockholders;

b. Power to govern the financial and operating policies of the enterprise under a statute or an agreement;

c. Power to appoint or remove the majority of the members of the board of directors or equivalent governing body; or

d. Power to cast the majority votes at meetings of the board of directors or equivalent governing body.

11. *External auditor* - means a single practitioner or a signing partner in an auditing firm.

12. *Auditing firm* – includes a proprietorship, partnership limited liability company, limited liability partnership, corporation (if any), or other legal entity, including any associated person of any of these entities, that is engaged in the practice of public accounting or preparing or issuing audit reports.

13. *Associate* – any director, officer, manager or any person occupying a similar status or performing similar functions in the audit firm including employees performing supervisory role in the auditing process.

14. *Partner* - all partners including those not performing audit engagements.

15. *Lead partner* – also referred to as engagement partner/partner-in-charge/ managing partner who is responsible for signing the audit report on the consolidated financial statements of the audit client, and where relevant, the individual audit report of any entity whose financial statements form part of the consolidated financial statements.

16. *Concurring partner* - the partner who is responsible for reviewing the audit report.

17. *Auditor-in-charge* – refers to the team leader of the audit engagement.

D. GENERAL CONSIDERATION AND LIMITATIONS OF THE SELECTION PROCEDURES

1. Subject to mutual recognition provision of the MOA and as implemented in this regulation, only external auditors and auditing firms included in the list of BSP selected external auditors and auditing firms shall be engaged by all the covered institutions detailed in Item *"B"*. The external auditor and/or auditing firm to be hired shall also be in-charge of the audit of the entity's subsidiaries and affiliates engaged in allied activities: *Provided,* That the external auditor and/or auditing firm shall be changed or the lead and concurring partner shall be rotated every five (5) years or earlier: *Provided further,* That the rotation of the lead and concurring partner shall have an interval of at least two (2) years.

2. Category A covered entities which have engaged their respective external auditors and/or auditing firm for a consecutive period of five (5) years or more as of 18 September 2009 shall have a one (1)-year period from said date within which to either change their external auditors and/or auditing firm or to rotate the lead and/or concurring partner.

3. The selection of the external auditors and/or auditing firm does not exonerate the covered institution or said auditors from their responsibilities. Financial statements filed with the BSP are still primarily the responsibility of the management of the reporting institution and accordingly, the fairness of the representations made therein is an implicit and integral part of the institution's responsibility. The independent certified public accountant's responsibility for the financial statements required to be filed with the BSP is confined to the expression of his opinion, or lack thereof, on such statements which he has audited/examined.

4. The BSP shall not be liable for any damage or loss that may arise from its selection of the external auditors and/or auditing firm to be engaged by banks for regular audit or non-audit services.

5. Pursuant to paragraph (5) of the MOA, SEC, BSP and IC shall mutually recognize the accreditation granted by any of them for external auditors and firms of Group C or D companies under SEC,

Category B and C under BSP, and insurance brokers under IC. Once accredited/selected by any one (1) of them, the above-mentioned special requirements shall no longer be prescribed by the other regulators.

For corporations which are required to submit financial statements to different regulators and are not covered by the mutual recognition policy of this MOA, the following guidance shall be observed:

a. The external auditors of UBs which are listed in the Exchange, should be selected/accredited by both the BSP and SEC, respectively; and

b. For insurance companies and banks that are not listed in the Exchange, their external auditors must each be selected/ accredited by BSP or IC, respectively. For purposes of submission to the SEC, the financial statements shall be at least audited by an external auditor registered/accredited with BOA.

This mutual recognition policy shall however be subject to the BSP restriction that for banks and its subsidiary and affiliate bank, QBs, trust entities, NSSLAs, their subsidiaries and affiliates engaged in allied activities and other FIs which under special laws are subject to BSP consolidated supervision, the individual and consolidated financial statements thereof shall be audited by only one (1) external auditor/auditing firm.

6. The selection of external auditors and/or auditing firm shall be valid for a period of three (3) years. The SES shall make an annual assessment of the performance of external auditors and/or auditing firm and will recommend deletion from the list even prior to the three (3)-year renewal period, if based on assessment, the external auditors' report did not comply with BSP requirements.

E. QUALIFICATION REQUIREMENT

The following qualification requirements are required to be met by the individual external auditor and the auditing firm at the time of application and on continuing basis, subject to BSP's provisions on the delisting and suspension of accreditation:

1. Individual external auditor

a. General requirements

(1) The individual applicant must be primarily accredited by the BOA. The individual external auditor or partner in-charge of the auditing firm must have at least five (5) years of audit experience.

(2) Auditor's independence.

In addition to the basic screening procedures of BOA on evaluating auditor's independence, the following are required for BSP purposes to be submitted in the form of notarized certification that:

(a) No external auditor may be engaged by any of the covered institutions under Item *"B"* hereof if he or any member of his immediate family had or has committed to acquire any direct or indirect financial interest in the concerned covered institution, or if his independence is considered impaired under the circumstances specified in the Code of Professional Ethics for CPAs. In case of a partnership, this limitation shall apply to the partners, associates and the auditor-in-charge of the engagement and members of their immediate family;

(b) The external auditor does not have/ shall not have outstanding loans or any credit accommodations or arranged for the extension of credit or to renew an extension of credit (except credit card obligations which are normally available to other credit card holders and fully secured auto loans and housing loans which are not past due) with the covered institutions under Item *"B"* at the time of signing the engagement and during the engagement. In the case of partnership, this prohibition shall apply to the partners and the auditor-in-charge of the engagement; and

(c) It shall be unlawful for an external auditor to provide any audit service to a covered institution if the covered

institution's CEO, CFO, Chief Accounting Officer (CAO), or comptroller was previously employed by the external auditor and participated in any capacity in the audit of the covered institution during the one-year preceding the date of the initiation of the audit;

(3) Individual applications as external auditor of entities under *Category A* above must have established adequate quality assurance procedures, such consultation policies and stringent quality control, to ensure full compliance with the accounting and regulatory requirements.

b. Specific requirements

(1) At the time of application, regardless of the covered institution, the external auditor shall have at least five (5) years experience in external audits;

(2) The audit experience above refers to experience required as an associate, partner, lead partner, concurring partner or auditor-in-charge; and

(3) At the time of application, the applicant must have the following track record:

(a) For *Category A,* he/she must have at least five (5) corporate clients with total assets of at least P50.0 million each.

(b) For *Category B,* he/she must have had at least three (3) corporate clients with total assets of at least P25.0 million each.

(c) For *Category C,* he/she must have had at least three (3) corporate clients with total assets of at least P5.0 million each;

2. Auditing firms

a. The auditing firm must be primarily accredited by the BOA and the name of the firm's applicant partner's should appear in the attachment to the certificate of accreditation issued by BOA. Additional partners of the firm shall be furnished by BOA to the concerned regulatory agencies (e.g. BSP, SEC and IC) as addendum to the firm's accreditation by BOA.

b. Applicant firms to act as the external auditor of entities under *Category A* in Item *"B"* must have established adequate quality assurance procedures, such consultation policies and stringent quality control, to ensure full compliance with the accounting and regulatory requirements.

c. At the time of application, the applicant firm must have at least one (1) signing practitioner or partner who is already selected/accredited, or who is already qualified and is applying for selection by BSP.

d. A registered accounting/auditing firm may engage in any non-auditing service for an audit client only if such service is approved in advance by the client's audit committee. Exemptions from the prohibitions may be granted by the Monetary Board on a case-by-case basis to the extent that such exemption is necessary or appropriate in the public interest. Such exemptions are subject to review by the BSP.

e. At the time of application, the applicant firm must have the following track record:

(1) For *Category A,* the applicant firm must have had at least twenty (20) corporate clients with total assets of at least P50.0 million each;

(2) For *Category B,* the applicant firm must have had at least five (5) corporate clients with total assets of at least P20.0 million each;

(3) For *Category C,* the applicant firm must have had at least five (5) corporate clients with total assets of at least P5.0 million each.

F. APPLICATION FOR AND/OR RENEWAL OF THE SELECTION OF INDIVIDUAL EXTERNAL AUDITOR

1. The initial application for BSP selection shall be signed by the external auditor and shall be submitted to the appropriate department of the SES together with the following documents/information:

a. Copy of effective and valid BOA Certificate of Accreditation with the attached list of qualified partner/s of the firm;

b. A notarized undertaking of the external auditor that he is in compliance with the qualification requirements under Item *"E"* and that the external auditor shall keep an audit or review working papers for at least seven (7) years in sufficient detail to support the conclusion in the audit report and making them available to the BSP's authorized representative/s when required to do so;

c. Copy of Audit Work Program which shall include assessment of the audited institution's compliance with BSP rules and regulations, such as, but not limited to the following:

(1) capital adequacy ratio, as currently prescribed by the BSP;

(2) AMLA framework;

(3) risk management system, particularly liquidity and market risks; and

(4) loans and other risk assets review and classification, as currently prescribed by the BSP rules and regulations.

d. If the applicant will have clients falling under *Category A,* copy of the Quality Assurance Manual which, aside from the basic elements as required under the BOA basic quality assurance policies and procedures, specialized quality assurance procedures should be provided consisting of, among other, review asset quality, adequacy of risk-based capital, risk management systems and corporate governance framework of the covered entities.

e. Copy of the latest AFS of the applicant's two (2) largest clients in terms of total assets.

2. Subject to BSP's provision on early deletion from the list of selected external auditor, the selection may be renewed within two (2) months before the expiration of the three (3)-year effectivity of the selection upon submission of the written application for renewal to the appropriate department of the SES together with the following documents/information:

(a) copy of updated BOA Certificate of Accreditation with the attached list of qualified partner/s of the firm;

(b) notarized certification of the external auditor that he still possess all qualification required under Item *"F.1.b"* of this Appendix;

(c) list of corporate clients audited during the three (3)-year period of being selected as external auditor by BSP. Such list shall likewise indicate the findings noted by the BSP and other regulatory agencies on said AFS including the action thereon by the external auditor; and

(d) written proof that the auditor has attended or participated in trainings for at least thirty (30) hours in addition to the BOA's prescribed training hours. Such training shall be in subjects like international financial reporting standards, international standards of auditing, corporate governance, taxation, code of ethics, regulatory requirements of SEC, IC and BSP or other government agencies, and other topics relevant to his practice, conducted by any professional organization or association duly recognized/accredited by the BSP, SEC or by the BOA/PRC through a CPE Council which they may set up.

The application for initial or renewal accreditation of an external auditor shall be accomplished by a fee of P2,000.00.

G. APPLICATION FOR AND/OR RENEWAL OF THE SELECTION OF AUDITING FIRMS

1. The initial application shall be signed by the managing partner of the auditing firm and shall be submitted to the appropriate department of the SES together with the following documents/information:

a. copy of effective and valid BOA Certificate of Accreditation with attachment listing the names of qualified partners;

b. notarized certification that the firm is in compliance with the general qualification requirements under Item *"E.2"*

and that the firm shall keep an audit or review working papers for at least seven (7) years insufficient detail to support the conclusions in the audit report and making them available to the BSP's authorized representative/s when required to do so;

c. copy of audit work program which shall include assessment of the audited institution's compliance with BSP rules and regulations, such as, but not limited to the following;

(1) capital adequacy ratio, as currently prescribed by the BSP;

(2) AMLA framework;

(3) risk management system, particularly liquidity and market risks; and

(4) loans and other risk assets review and classification, as currently prescribed by the BSP rules and regulations.

d. If the applicant firm will have clients falling under *Category A,* copy Quality Assurance Manual where, aside from the basic elements as required under the BOA basic quality assurance policies and procedures, specialized quality assurance procedures should be provided relative to, among others review asset quality, adequacy of risk-based capital, risk management systems and corporate governance framework of covered entities;

e. Copy of the latest AFS of the applicant's two (2) largest clients in terms of total assets; and

f. Copy of firm's AFS for the immediately preceding two (2) years.

2. Subject to BSP's provision on early deletion from the list of selected auditing firm, the selection may be renewed within two (2) months before the expiration of the three (3)-year effectivity of the selection upon submission of the written application for renewal to the appropriate department of the SES together with the following documents/information:

a. a copy of updated BOA Certificate of Registration with the attached list of qualified partner/s of the firm;

b. amendments on Quality Assurance Manual, inclusive of written explanation on such revision, if any; and

c. notarized certification that the firm is in compliance with the general qualification requirements under Item *"G.1.b"* hereof;

The application for initial or renewal accreditation of an auditing firm shall be accompanied by a fee of P5,000.00.

H. REPORTORIAL REQUIREMENTS

1. To enable the BSP to take timely and appropriate remedial action, the external auditor and/or auditing firm must report to the BSP within thirty (30) calendar days after discovery, the following cases:

a. Any material finding involving fraud or dishonesty (including cases that were resolved during the period of audit);

b. Any potential losses the aggregate of which amounts to at least one percent (1%) of the capital;

c. Any finding to the effect that the consolidated assets of the company, on a going concern basis, are no longer adequate to cover the total claims of creditors; and

d. Material internal control weaknesses which may lead to financial reporting problems.

2. The external auditor/auditing firm shall report directly to the BSP within fifteen (15) calendar days from the occurrence of the following:

a. Termination or resignation as external auditor and stating the reason therefor;

b. Discovery of a material breach of laws or BSP rules and regulations such as, but not limited to:

(1) CAR; and

(2) Loans and other risk assets review and classification.

c. Findings on matters of corporate governance that may require urgent action by the BSP.

3. In case there are no matters to report (e.g. fraud, dishonesty, breach of laws, etc.) the external auditor/auditing firm shall submit directly to BSP within fifteen (15) calendar days after the closing of the audit engagement a notarized certification that there is none to report.

The management of the covered institutions, including its subsidiaries and affiliates, shall be informed of the adverse findings and the report of the external auditor/auditing firm to the BSP shall include pertinent explanation and/or corrective action.

The management of the covered institutions, including its subsidiaries and affiliates, shall be given the opportunity to be present in the discussions between the BSP and the external auditor/auditing firm regarding the audit findings, except in circumstances where the external auditor believes that the entity's management is involved in fraudulent conduct.

It is, however, understood that the accountability of an external auditor/ auditing firm is based on matters within the normal coverage of an audit conducted in accordance with generally accepted auditing standards and identified non-audit services.

I. DELISTING AND SUSPENSION OF SELECTED EXTERNAL AUDITOR/ AUDITING FIRM

1. An external auditor's duly selected pursuant to this regulation shall be suspended or delisted, in a manner provided under this regulation, under any of the following grounds:

a. Failure to submit the report under Item *"H"* of this Appendix or the required reports under Subsec. X190.1;

b. Continuous conduct of audit despite loss of independence as provided under Item *"E.1"* or contrary to the requirements under the Code of Professional Ethics;

c. Any willful misrepresentation in the following information/documents;

(1) application and renewal for accreditation;

(2) report required under Item *"H"*; and

(3) Notarized certification of the external auditor and/or auditing firm.

d. The BOA found that, after due notice and hearing, the external auditor committed an act discreditable to the profession as specified in the Code of Professional Ethics for CPAs. In this case, the BOA shall inform the BSP of the results thereof;

e. Declaration of conviction by a competent court of a crime involving moral turpitude, fraud (as defined in the Revised Penal Code), or declaration of liability for violation of the banking laws, rules and regulation, the Corporation Code of the Philippines, the Securities Regulation Code (SRC); and the rules and regulations of concerned regulatory authorities;

f. Refusal for no valid reason, upon lawful order of the BSP, to submit the requested documents in connection with an ongoing investigation. The external auditor should however been made aware of such investigation;

g. Gross negligence in the conduct of audits which would result, among others, in non-compliance with generally accepted auditing standards in the Philippines or issuance of an unqualified opinion which is not supported with full compliance by the auditee with generally accepted accounting principles in the Philippines (GAAP). Such negligence shall be determined by the BSP after proper investigation during which the external auditor shall be given due notice and hearing;

h. Conduct of any of the non-audit services enumerated under Item *"E.1"* for his statutory audit clients, if he has not undertaken the safeguards to reduce the threat to his independence; and

i. Failure to comply with the Philippine Auditing Standards and Philippine Auditing Practice Statements.

2. An auditing firms; accreditation shall be suspended or delisted, after due notice and hearing, for the following grounds:

a. Failure to submit the report under Item *"H"* or the required reports under Sec. X190.1.

b. Continuous conduct of audit despite loss of independence of the firm as provided under this regulation and under the Code of Professional Ethics;

c. Any willful misrepresentation in the following information/ documents;

(1) Application and renewal for accreditation;

(2) Report required under Item *"H"*; and

(3) Notarized certification of the managing partner of the firm.

d. Dissolution of the auditing firm/ partnership, as evidenced by an Affidavit of Dissolution submitted to the BOA, or upon findings by the BSP that the firm/ partnership is dissolved. The accreditation of such firm/partnership shall however be reinstated by the BSP upon showing that the said dissolution was solely for the purpose of admitting new partner/s have complied with the requirements of this regulation and thereafter shall be reorganized and re-registered;

e. There is a showing that the accreditation of the following number or percentage of external auditors, whichever is lesser, have been suspended or delisted for whatever reason, by the BSP:

(1) at least ten (10) signing partners and currently employed selected/accredited external auditors, taken together; or

(2) such number of external auditors constituting fifty percent (50%) or more of the total number of the firm's signing partners and currently selected/accredited auditors, taken together.

f. The firm or any one (1) of its auditors has been involved in a major accounting/ auditing scam or scandal. The suspension or delisting of the said firm shall depend on the gravity of the offense or the impact of said scam or scandal on the investing public or the securities market, as may be determined by the BSP;

g. The firm has failed reasonably to supervise an associated person and employed auditor, relating to the following:

(1) auditing or quality control standards, or otherwise, with a view to preventing violations of this regulations;

(2) provisions under SRC relating to preparation and issuance of audit reports and the obligations and liabilities of accountants with respect thereto;

(3) the rules of the BSP under this Appendix; or

(4) professional standards.

h. Refusal for no valid reason, upon order of the BSP, to submit requested documents in connection with an ongoing investigation. The firm should however be made aware of such investigation.

3. Pursuant to paragraph 8 of the aforesaid MOA, the SEC, BSP and IC shall inform BOA of any violation by an accredited/selected external auditor which may affect his/her accreditation status as a public practitioner. The imposition of sanction by BOA on an erring practitioner shall be without prejudice to the appropriate penalty that the SEC, IC or BSP may assess or impose on such external auditor pursuant to their respective rules and regulations. In case of revocation of accreditation of a public practitioner by BOA, the accreditation by SEC, BSP and IC shall likewise be automatically revoked/derecognized.

The SEC, BSP and IC shall inform each other of any violation committed by an external auditor who is accredited/selected by any one (1) or all of them. Each agency shall undertake to respond on any referral or endorsement by another agency within ten (10) working days from receipt thereof.

4. Procedure and Effects of Delisting/ Suspension.

a. An external auditor/auditing firm shall only be delisted upon prior notice to him/it and after giving him/it the opportunity to be heard and defend himself/itself by presenting witnesses/ evidence in his favor. Delisted external auditor and/or auditing firm may re-apply for BSP selection after the period prescribed by the Monetary Board.

b. BSP shall keep a record of its proceeding/investigation. Said proceedings/ investigation shall not be public, unless otherwise ordered by the Monetary Board for good cause shown, with the consent of the parties to such proceedings.

c. A determination of the Monetary Board to impose a suspension or delisting under this section shall be supported by a clear statement setting forth the following:

(1) Each act or practice in which the selected/accredited external auditor or auditing firm, or associated entry, if applicable, has engaged or omitted to engage, or that forms a basis for all or part of such suspension/delisting;

(2) The specific provision/s of this regulation, the related SEC rules or professional standards which the Monetary Board determined as has been violated; and

(3) The imposed suspension or delisting, including a justification for either sanction and the period and other requirements specially required within which the delisted auditing firm or external auditor may apply for re-accreditation.

d. The suspension/delisting, including the sanctions/penalties provided in Sec. X189 shall only apply to:

(1) Intentional or knowing conduct, including reckless conduct, that results in violation or applicable statutory, regulatory or professional standards; or

(2) Repeated instances of negligent conduct, each resulting in a violation of the applicable statutory, regulatory or professional standards.

e. No associate person or employed auditor of a selected/accredited auditing firm shall be deemed to have failed reasonably to supervise any other person for purpose of Item *"I.2.g"* above, if:

(1) There have been established in and for that firm procedures, and a system for applying such procedures, that comply with applicable rules of BSP and that would reasonably be expected to prevent and detect any such violation by such associated person; and

(2) Such person or auditor has reasonably discharged the duties and obligations incumbent upon that person by reason of such procedures and system, and had no reasonable cause to believe that such procedures and system were not being complied with.

f. The BSP shall discipline any selected external auditor that is suspended or delisted from being associated with any selected auditing firm, or for any selected auditing firm that knew, or in the exercise or reasonable care should have known, of the suspension or delisting of any selected external auditor, to permit such association, without the consent of the Monetary Board.

g. The BSP shall discipline any covered institution that knew or in the exercise of reasonable care should have known, of the suspension or delisting of its external auditor or auditing firm, without the consent of the Monetary Board.

h. The BSP shall establish for appropriate cases an expedited procedure for consideration and determination of the question of the duration of stay of any such disciplinary action pending review of any disciplinary action of the BSP under this Section.

J. SPECIFIC REVIEW

When warranted by supervisory concern, the Monetary Board may, at the expense of the covered institution require the external auditor and/or auditing firm to undertake a specific review of a particular

aspect of the operations of these institutions. The report shall be submitted to the BSP and the audited institution simultaneously, within thirty (30) calendar days after the conclusion of said review.

K. AUDIT BY THE BOARD OF DIRECTORS

Pursuant to Section 58 of RA. No. 8791, otherwise known as "The General Banking Law of 2000" the Monetary Board may also direct the board of directors of a covered institution or the individual members thereof, to conduct, either personally or by a committee created by the board, an annual balance sheet audit of the covered institution to review the internal audit and the internal control system of the concerned entity and to submit a report of such audit to the Monetary Board within thirty (30) calendar days after the conclusion thereof.

L. AUDIT ENGAGEMENT

Covered institutions shall submit the audit engagement contract between them, their subsidiaries and affiliates and the external auditor/auditing firm to the appropriate department of the SES within fifteen (15) calendar days from signing thereof. Said contract shall include the following provisions:

1. That the covered institution shall be responsible for keeping the auditor fully informed of existing and subsequent changes to prudential regulatory and statutory requirements of the BSP and that both parties shall comply with said requirements;
2. That disclosure of information by the external auditor/auditing firm to the BSP as required under Items *"H"* and *"J"* hereof, shall be allowed; and
3. That both parties shall comply with all the requirements under this Appendix.

(As amended by Circular No. 660 dated 25 August 2009)

QUALIFICATION REQUIREMENTS FOR A BANK/NON-BANK FINANCIAL INSTITUTION APPLYING FOR ACCREDITATION TO ACT AS TRUSTEE ON ANY MORTGAGE OR BOND ISSUED BY ANY MUNICIPALITY, GOVERNMENT-OWNED OR CONTROLLED CORPORATION, OR ANY BODY POLITIC

(Appendix to Subsec. 4409Q.16)

A bank/NBFI applying for accreditation to act as trustee on any mortgage or bond issued by any municipality, government-owned or controlled corporation, or any body politic must comply with the following requirements:

a. It must be a bank or NBFI under BSP supervision;

b. It must have a license to engage in trust and other fiduciary business;

c. It must have complied with the minimum capital accounts required under existing regulations, as follows:

UBs and KBs	The amount required under existing regulations or such amount as may be required by the Monetary Board in the future
Branches of Foreign Banks	The amount required under existing regulations
Thrift Banks	₱650 million or such amounts as may be required by the Monetary Board in the future
NBFIs	Adjusted capital of at least ₱300.0 million or such amounts as may be required by the Monetary Board in the future.

d. Its risk-based capital adequacy ratio is not lower than twelve percent (12%) at the time of filing the application;

e. The articles of incorporation or governing charter of the institution shall include among its powers or purposes, acting as trustee or administering any trust or holding property in trust or on deposit for the use, or in behalf of others;

f. The by-laws of the institution shall include among others, provisions on the following:

(1) The organization plan or structure of the department, office or unit which shall conduct the trust and other fiduciary business of the institution;

(2) The creation of a trust committee, the appointment of a trust officer and subordinate officers of the trust department; and

(3) A clear definition of the duties and responsibilities as well as the line and staff functional relationships of the various units, officers and staff within the organization.

g. The bank's operation during the preceding calendar year and for the period immediately preceding the date of application has been profitable;

h. It has not incurred net weekly reserve deficiencies during the eight (8) weeks period immediately preceding the date of application;

i. It has generally complied with banking laws, rules and regulations, orders or instructions of the Monetary Board and/or BSP Management in the last two preceding examinations prior to the date of application, particularly on the following:

(1) election of at least two (2) independent directors;

(2) attendance by every member of the board of directors in a special seminar for board of directors conducted or accredited by the BSP;

(3) the ceilings on credit accommodations to DOSRI;

(4) liquidity floor requirements for government deposits;

(5) single borrower's loan limit; and

(6) investment in bank premises and other fixed assets.

j. It maintains adequate provisions for probable losses commensurate to the quality of its assets portfolio but not lower than the required valuation reserves as determined by the BSP;

k. It does not have float items outstanding for more than sixty (60) calendar days in the "Due From/To Head Office/Branches/Other Offices" accounts and the "Due from Bangko Sentral" account exceeding one percent (1%) of the total resources as of date of application;

l. It has established a risk management system appropriate to its operations characterized by clear delineation of responsibility for risk management, adequate risk measurement systems, appropriately structured risk limits, effective internal controls and complete, timely and efficient risk reporting system;

m. It has a CAMELS Composite Rating of at least "3" in the last regular examination with management rating of not lower than "3"; and

n. It is a member of the PDIC in good standing (for banks only).

Compliance with the foregoing as well as with other requirements under existing regulations shall be maintained up to the time the trust license is granted. A bank that fails in this respect shall be required to show compliance for another test period of the same duration.

RULES AND REGULATIONS ON COMMON TRUST FUNDS[1]

(Appendix to Sec. 4410Q)

1. The administration of CTFs shall be subject to the provisions of Subsecs. 4409Q.1 up to 4409Q.6 and to the following regulations.

As an alternative compliance with the required prior authority and disclosure under Subsecs. 4409Q.2 and 4409Q.3, a list which shall be updated quarterly of prospective and/or outstanding investment outlets may be made available by the trustee for the review of all CTF clients. *(Sec. 4410Q)*

2. Establishment of CTFs. Any trust company or investment house authorized to engage in trust business may establish, administer and maintain one (1) or more CTFs. *(Subsec. 4410Q.1)*

3. Minimum documentary requirements for CTFs. In addition to the trust agreement or indenture required under Subsec. 4409Q.1, each CTF shall be established, administered and maintained in accordance with a written declaration of trust referred to as the plan, which shall be approved by the board of directors of the trustee and a copy submitted to the appropriate department of the SES within thirty (30) business days prior to its implementation.

The plan shall make provisions on the following matters:

a. Title of the plan;

b. Manner in which the plan is to be operated;

c. Investment powers of the trustee with respect to the plan, including the character and kind of investments which may be purchased;

d. Allocation, apportionment and distribution dates of income, profit and losses;

e. Terms and conditions governing the admission or withdrawal as well as expansion or contraction of participations in the plan including the minimum initial placement and account balance to be maintained by the trustor;

f. Auditing and settlement of accounts of the trustee with respect to the plan;

g. Detailed information on the basis, frequency, and method of valuing and accounting of CTF assets and each participation in the fund;

h. Basis upon which the plan may be terminated;

i. Liability clause of the trustee;

j. Schedule of fees and commissions which shall be uniformly applied to all participants in a fund and which shall not be changed between valuation dates; and

k. Such other matters as may be necessary or proper to define clearly the rights of participants under the plan.

The legal capacity of the institution administering a CTF shall be indicated in the plan and other related agreements or contracts as trustee of the fund and not in any other capacity such as fund manager, financial manager, or like terms.

The provisions of the plan shall control all participations in the fund and the rights and benefits of all parties in interest.

The plan may be amended by resolution of the board of directors of the trustee: *Provided, however*, That participants in the fund shall be immediately notified of such amendments and shall be allowed to

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[1] The rules and regulations on CTFs were previously under Sec. 4410Q and the subsections enclosed in parentheses.The UIT Funds regulations which are now in said section/subsections took effect on 01 October 2004 (effectivity of Circular No. 447 dated 03 September 2004).

withdraw their participations if they are not in conformity with the amendments made: *Provided, further,* That amendments to the plan shall be submitted to the appropriate department of the SES within ten (10) business days from approval of the amendments by the board of directors.

A copy of the plan shall be available at the principal office of the trustee during regular office hours for inspection by any person having an interest in a trust whose funds are invested in the plan or by his authorized representative. Upon request, a copy of the plan shall be furnished such person. *(Subsec. 4410Q.2)*

4. Management of CTFs. The trustee shall have the exclusive management and control of each CTF administered by it, and the sole right at any time to sell, convert, reinvest, exchange, transfer or otherwise change or dispose of the assets comprising the fund.

The trustee shall designate clearly in its records the trust accounts owning participation in the CTF and the extent of the interests of such account. The trustee shall not negotiate nor assign the trustor's beneficial interest in the CTF without prior written consent of the trustor or beneficiary. No trust account holding a participation in a CTF shall have or be deemed to have any ownership or interest in any particular asset or investment in the CTF but shall have only its proportionate beneficial interest in the fund as a whole. *(Subsec. 4410Q.3)*

5. Trustee as participant in CTFs. A trustee administering a CTF shall not have any interest in such fund other than in its capacity as trustee of the CTF nor grant any loan on the security of a participation in such fund: *Provided, however,* That a trustee which administers funds representing employee benefit plans under trust or investment management may invest funds in the CTF: *Provided, further,* That in the case of employee benefit plans under trust belonging to employees of entities other than that of the trustee, the trustee may invest such funds in its own CTF only on a temporary basis in accordance with Subsec. 4409Q.5. *(Subsec. 4410Q.4)*

6. Exposure limit of CTF to a single person or entity. No investment for a CTF shall be made in stocks, bonds, bank deposits or other obligations of any one (1) person, firm or corporation, if as a result of such investment the total amount invested in stocks, bonds, bank deposits or other obligations issued or guaranteed by such person, firm or corporation shall aggregate to an amount in excess of fifteen percent (15%) of the market value of the CTF: *Provided*, That this limitation shall not apply to investments in government securities or other evidences of indebtedness of the Republic of the Philippines and of the BSP, and any other evidences of indebtedness or obligations the servicing and repayment of which are fully guaranteed by the Republic of the Philippines. *(Subsec. 4410Q.5)*

7. Operating and accounting methodology. By its inherent nature, a CTF shall be operated and accounted for in accordance with the following:

a. The trustee shall have exclusive management and control of each CTF administered by it and the sole right at any time to sell, convert, reinvest, exchange, transfer or otherwise change or dispose of the assets comprising the fund;

b. The total assets and accountabilities of each fund shall be accounted for as a single account referred to as *pooled fund accounting;*

c. Contributions to each fund by clients shall always be through participations in the fund;

d. All such participations shall be pooled and invested as one (1) account (referred to as collective investments); and

e. The interest of each participant shall be determined by a formal method of participation valuation established in the written plan of the CTF, and no participation shall be admitted to or withdrawn from the fund except on the basis of such valuation. *(Subsec. 4410Q.6)*

8. Tax-exempt common trust funds The following shall be the features/ requirements of CTFs which may qualify for exemption from the twenty percent (20%) final tax under Section 24(B)(1) of R.A. No. 8424 (The Tax Reform Act of 1997):

a. The tax exemption shall apply to CTFs established on or after January 3, 2000;

b. The CTF indenture or plan as well as evidences of participation shall clearly indicate that the participants shall be limited to individual trustors/investors who are Filipino citizens or resident aliens and that participation is non-negotiable and non-transferable;

c. The date of contributions to the CTF shall be clearly indicated in the evidence of participation to serve as basis for the trustee-QB to determine the period of participation for tax exemption purposes;

d. The CTF indenture/plan as well as the evidence of participation shall indicate that pursuant to Section 24(B)(1) of R.A. No. 8424, interest income of the CTF derived from investments in interest-bearing instruments (e.g., time deposits, government securities, loans and other debt instruments) which are otherwise subject to the twenty percent (20%) final tax, shall be exempt from said final tax provided participation in the CTF is for a period of at least five (5) years. If participation is for a period less than five (5) years, interest income shall be subject to a final tax which shall be deducted and withheld based on the following schedule:

Participation Period	Rate of Tax
Four (4) years to less than five (5) years	5%
Three (3) years to less than four (4) years	12%
Less than three (3) years	20%

Necessarily, the date of contribution shall be clearly indicated in the evidence of participation which shall serve as basis for determining the participation period of each participant; and

e. Tax-exempt CTFs established under this Subsection shall be subject to the provisions of Subsecs. 4409Q.1(c), 4409Q.2 up to 4409Q.7, and Items *"2 to 7"* of this Appendix.

Regarding the required prior authority and disclosure under Subsecs. 4409Q.2 and 4409Q.3, a list of prospective and/or outstanding investment outlets that is made available by the trustee for the review of all CTF clients may serve as an alternative compliance, which list shall be updated quarterly. *(Subsec. 4410Q.7)*

9. Custody of Securities. Investments in securities of all existing CTFs shall be delivered to a BSP-accredited third party custodian not later than 31 October 2004.

CHECKLIST OF BSP REQUIREMENTS IN THE SUBMISSION OF FINANCIAL AUDIT REPORT, ANNUAL AUDIT REPORT AND REPORTS REQUIRED UNDER APPENDIX Q-30

[Appendix to Secs. 4190Q (2008 - 4172Q), 4172S and 4172N]

The external auditor (Included in the List of BSP Selected External Auditors) shall start the audit not later than thirty (30) calendar days after the close of the calendar/fiscal year adopted by the bank. AFS of banks/QBs with subsidiaries shall be presented side by side on a solo basis and on a consolidated basis (QBs and subsidiaries). The FAR shall be submitted by the bank/QB to the appropriate department of the SES not later than 120 calendar days after the close of the calendar year or fiscal year adopted by the bank/QB, together with the following:

Information/Data Required	Deadline for submission
A. FAR	
1. Certification by the external auditor on the following:	For submission together with the FAR not later than 120 calendar days after the close of the calendar year or fiscal year adopted by the bank.
a. The dates of commencement and termination of audit.	
b. The date when the FAR and certification under oath stating that no material weakness or breach in the internal control and risk management systems was noted in the course of the audit of the bank/QB were submitted to the board of directors or country head, in the case of foreign bank branches; and	
c. That the external auditor, partners, associates, auditor-in-charge of the engagement and the members of their immediate family do not have any direct or indirect financial interest with the bank/QB, its subsidiaries and affiliates and that their independence is not considered impaired under the circumstances specified in the Code of Professional Ethics for CPAs.	
2. Reconciliation statement for the differences in amounts between the audited and the submitted BS and IS for bank proper (regular and FCDU) and	For submission together with the FAR not later than 120 calendar days after the close of the calendar year or fiscal year adopted by the bank.

Information/Data Required	Deadline for submission
trust department, including copies of adjusting entries on the reconciling items. **Note:** Please see pro-forma comparative analysis (Annex Q-33-a).	
3. LOC indicating the external auditor's findings and comments on the material weakness noted in the internal control and risk management systems and other aspects of operations.	Within thirty (30) calendar days after submission of the FAR.
In case no material weakness is noted to warrant the issuance of an LOC, a certification under oath stating that no material weakness or breach in the internal control and risk management systems was noted in the course of the audit of the bank shall be submitted by the external auditor.	For submission together with the FAR not later than 120 calendar days after the close of the calendar year or fiscal year adopted by the bank.
4. Copies of the board resolutions showing the:	
a. Action taken on the FAR and, where applicable, on the certification under oath including the names of the directors, present and absent, among other things; and	Within thirty (30) banking days after the receipt of the FAR and certification under oath by the board of directors.
b. Action taken on the findings and recommendations in the LOC, and the names of the directors present and absent, among other things.	Within thirty (30) banking days after the receipt of the LOC by the board of directors.
5. In case of foreign banks with branches in the Philippines, in lieu of the board resolution:	
a. A report by the country head on the action taken by management (head office, regional or country) on the FAR and, where applicable, on the	Within thirty (30) banking days after the receipt of the FAR and certification under oath by the country head.

Information/Data Required	Deadline for submission
applicable, on certification under oath stating that no material weakness or breach in the internal control and risk management systems was noted in the course of the audit of the bank.	
b. A report by the country head on the action taken by management (head office, regional or country) on the LOC.	Within thirty (30) banking days after the receipt of the LOC by the country head.
6. Certification of the external auditor on the date when the LOC was submitted to the board of directors or country head.	Within thirty (30) banking days after the receipt of the LOC by the board of directors or country head.
7. All the required disclosures in the AFS provided under Subsec. 4190Q.4	For submission together with the FAR not later than one hundred twenty calendar days after the close of the calendar year or fiscal year adopted by the bank.
8. Reports required to be submitted by the external auditor under *Appendix Q-30*.	
a. To enable the BSP to take timely and appropriate remedial action, the external auditor must report to the BSP, the following cases: (1) Any material finding involving fraud or dishonesty (including cases that were resolved during the period of audit); and (2) Any potential losses the aggregate of which amounts to at least one percent (1%) of the capital.	Within thirty (30) calendar days after discovery.
b. The external auditor shall report directly to the BSP the following: (1) Termination or resignation as external auditor and starting the reason therefore; (2) Discovery of a material breach of laws or BSP rules and regulations such as, but not limited to:	Within fifteen (15) calendar days after the occurrence/discovery.

Information/Data Required	Deadline for submission
(a) CAR; and (b) Loans and other risk assets review and classification.	
(3) Findings on matters of corporate governance that may require urgent action by the BSP.	
c. In case there are no matters to report (e.g., fraud, dishonesty, breach of laws, etc.) a notarized certification that there is none to report.	Within fifteen (15) calendar days after the closing of the audit engagement.
B. AAR – For banks and other FIs under the concurrent jurisdiction of the BSP and COA.	
1. Copy of the AAR accompanied by the:	Within thirty (30) banking days after receipt of the AAR by the board of directors.
a. Certification by the institution concerned on the date of receipt of the AAR by the board of directors;	
b. Reconciliation statement between the AFS in the AAR and the BS and IS of bank proper (Regular and FCDU) and trust department submitted to the BSP, including copies of adjusting entries on the reconciling items; and	
c. Other information that may be required by the BSP.	
2. Copy of the board resolution showing the action taken on the AAR, as well as on the comments and observations, including the names of the directors present and absent, among other things.	Within thirty (30) banking days after receipt of the AAR by the board of directors.

(As amended by Circular Nos. 554 dated 22 December 2006 and 540 dated 09 August 2006)

Annex Q-33-a

Name of Financial Institution
Comparison of Submitted Consolidated Balance Sheet and Income Statement
and Audited Financial Statements
(Parent and Subsidiaries)
As of (end of calendar or fiscal year)
(In Thousand Pesos)

	Submitted Report	Audited Report	Variance/ Discrepancy	Reasons for Discrepancy
Cash and Other Cash Items				
Due from BSP				
Due from Other Banks				
Financial Assets Held for Trading (HFT)				
Held-to-Maturity (HTM) Financial Assets				
Available-for-Sale Financial Assets				
Loans and Receivables, *net*				
Interbank Loans Receivable				
Equity Investments in Subsidiaries, Associates & Joint Ventures				
Bank Premises, Furniture, Fixtures and Equipment, net				
Real and Other Properties Acquired (ROPA), net				
Other Assets				
Due from Head Office/Branches/Agencies Abroad				
Total Assets				
Deposit Liabilities				
Bills Payable				
Bonds Payable				
Unsecured Subordinated Debt (UnSD)				
Redeemable Preferred Shares				
Accrued Interest, Taxes and Other Expenses				
Other Liabilities				
Due to Head Office/Branches/Agencies Abroad				
Total Liabilities				
Paid-in Capital Stock				
Additional Paid-In Capital				
Retained Earnings				
Assigned Capital				
Total Capital				
Total Liabilities and Capital				
Total Income				
Total Expenses				
Net Income before Income Tax				

(As amended by Circular Nos. 554 dated 22 December 2006 and 540 dated 09 August 2006)

QUARTERLY INVESTMENT DISCLOSURE STATEMENT
(Appendix to Subsec. 4410Q.7)

Name of Unit Investment Trust Fund:
For the Quarter ended:
Net Asset Value, end of quarter:
Net Asset Value Per Unit (NAVPu):

Short Description:

(e.g., The Fund is a peso denominated fixed-income fund. The investment objective of the Fund is to generate a steady stream of income by investing in a diversified portfolio of high-grade marketable securities)

Administrative Details:

Trust Fee:
Minimum Investment:
Holding Period:
Participation/Redemption Conditions:
Special Reimbursable Expenses, if any:

Outstanding Investments:

The Fund has investments in the following:

(may be in graph format showing weightings per investment type or class of security)

Prospective Investments:

The following names/securities are among the fund's approved investment outlets where the Trustee intends to invest in depending on its availability or other market driven circumstances:

Annex A

(NAME OF TRUST ENTITY)-(TRUST BANKING GROUP/TRUST DEPARTMENT)
Unit Investment Trust Funds
RISK DISCLOSURE STATEMENT

Prior to making an investment in any of the (Name of Trust Entity) Unit Investment Trust Funds (UITFs), (Name of Trust Entity) is hereby informing you of the nature of the UITFs and the risks involved in investing therein. As investments in UITFs carry different degrees of risk, it is necessary that before you participate/invest in these funds, you should have: 1. Fully understood the nature of the investment in UITFs and the extent of your exposure to risks; 2. Read this Risk disclosure Statement completely; and 3. Independently determined that the investment in the UITFs is appropriate for you.

There are risks involved in investing in the UITFs because the value of your investment is based on the Net Asset Value per unit (NAVpu) of the Fund which uses a marked-to-market valuation and therefore may fluctuate daily. The NAVpu is computed by dividing the Net Asset Value (NAV) of the Fund by the number of outstanding units. The NAV is derived from the summation of the market value of the underlying securities of the Fund plus accrued interest income less liabilities and qualified expenses.

Investment in the UITF does not provide guaranteed returns even if invested in government securities and high-grade prime investment outlets. Your principal and earnings from investment in the Fund can be lost in whole or in part when the NAVpu at the time of redemption is lower than the NAVpu at the time of participation. Gains from investment is realized when the NAVpu at the time of redemption is higher than the NAVpu at the time of participation.

Your investment in any of the (Name of Trust Entity) UITFs exposes you to the various types of risks enumerated and defined hereunder:

Interest Rate Risk. This is the possibility for an investor to experience losses due to changes in interest rates. The purchase and sale of a debt instrument may result in profit or loss because the value of a debt instrument changes inversely with prevailing interest rates.

The UITF portfolio, being market-to-market, is affected by changes in interest rates thereby affecting the value of fixed income investments such as bonds. Interest rate changes may affect the prices of fixed income securities inversely, i.e., as interest rates rise, bond prices fall and when interest rates decline, bond prices rise. As the prices of bonds in a Fund adjust to a rise in interest rates, the Fund's unit price may decline.

Market/Price Risk. This is the possibility for an investor to experience losses due to changes in market prices of securities (e.g., bonds and equities). It is the exposure to the uncertain market value of a portfolio due to price fluctuations.

It is the risk of the UITF to lose value due to a decline in securities prices, which may sometimes happen rapidly or unpredictably. The value of investments fluctuates over a given time period because of general market conditions, economic changes or other events that impact large portions of the market such as political events, natural calamities, etc. As a result, the NAVpu may increase to make profit or decrease to incur loss.

Liquidity Risk. This is the possibility for an investor to experience losses due to the inability to sell or convert assets into cash immediately or in instances where conversion to

cash is possible but at a loss. These may be caused by different reasons such as trading in securities with small or few outstanding issues, absence of buyers, limited buy/sell activity or underdeveloped capital market.

Liquidity risk occurs when certain securities in the UITF portfolio may be difficult or impossible to sell at a particular time which may prevent the redemption of investment in UITF until its assets can be converted to cash. Even government securities which are the most liquid of fixed income securities may be subjected to liquidity risk particularly if a sizeable volume is involved.

Credit Risk/Default Risk. This is the possibility for an investor to experience losses due to a borrower's failure to pay principal and/or interest in a timely manner on instruments such as bonds, loans, or other forms of security which the borrower issued. This inability of the borrower to make good on its financial obligations may have resulted from adverse changes in its financial condition thus, lowering credit quality of the security, and consequently lowering the price (market/price risk) which contributes to the difficulty in selling such security. It also includes risk on a counterparty (a party the UITF Manager trades with) defaulting on a contract to deliver its obligation either in cash or securities.

This is the risk of losing value in the UITF portfolio in the event the borrower defaults on his obligation or in the case of a counterparty, when it fails to deliver on the agreed trade. This decline in the value of the UITF happens because the default/failure would make the price of the security go down and may make the security difficult to sell. As these happen, the UITFs NAVpu will be affected by a decline in value.

Reinvestment Risks. This is the risk associated with the possibility of having lower returns or earnings when maturing funds or the interest earnings of funds are reinvested.

Investors in the UITF who redeem and realize their gains run the risk of reinvesting their funds in an alternative investment outlet with lower yields. Similarly, the UITF manager is faced with the risk of not being able to find good or better alternative investment outlets as some of the securities in the fund matures.

In case of a foreign-currency denominated UITF or a peso denominated UITF allowed to invest in securities denominated in currencies other than its base currency, the UITF is also exposed to the following risks:

Foreign Exchange Risk. This is the possibility for an investor to experience losses due to fluctuations in foreign exchange rates. The exchange rates depend upon a variety of global and local factors, e.g., interest rates, economic performance, and political developments.

It is the risk of the UITF to currency fluctuations when the value of investments in securities denominated in currencies other than the base currency of the UITF depreciates. Conversely, it is the risk of the UITF to lose value when the base currency of the UITF appreciates. The NAVpu of a peso-denominated UITF invested in foreign currency-denominated securities may decrease to incur loss when the peso appreciates.

Country Risk. This is the possibility for an investor to experience losses arising from investments in securities issued by/in foreign countries due to the political, economic and social structures of such countries. There are risks in foreign investments due to the possible internal and external conflicts, currency devaluations, foreign ownership limitations and tax increases of the foreign country involved which are difficult to predict but must be taken into account in making such investments.

Likewise, brokerage commissions and other fees may be higher in foreign securities. Government supervision and regulation of foreign stock exchanges, currency markets, trading systems and brokers may be less than those in the Philippines. The procedures and rules governing foreign transactions and custody of securities may also involve delays in payment, delivery or recovery of investments.

Other Risks. Your participation in the UITFs may be further exposed to the risk of any actual or potential conflicts of interest in the handling of in-house or related party transactions by (Name of Trust Entity). These transactions may include own-bank deposits; purchase of own-institution or affiliate obligations (stock, mortgages); purchase of assets from or sales to own institution, directors, officers, subsidiaries, affiliates or other related interests/parties; or purchases or sales between fiduciary/managed accounts.

I/we have completely read and fully understood this risk disclosure statement and the same was clearly explained to me/us by a (Name of Trust Entity) UIT marketing personnel before I/we affixed my/our signature/s herein. I/we hereby voluntarily and willingly agree to comply with any and all laws, regulations, the plan rules, terms and conditions governing my/our investment in the (Name of Trust Entity) UITFs.

Signature over Printed Name	Date

I acknowledge that I have (1) advised the client to read this Risk Disclosure Statement, (2) encouraged the client to ask questions on matters contained in this Risk Disclosure Statement, and (3) fully explained the same to the client.

Signature over Printed Name/ Position of UIT Marketing Personnel	Date

(Circular No. 593 dated 08 January 2008)

BANGKO SENTRAL RULES OF PROCEDURE ON ADMINISTRATIVE CASES INVOLVING DIRECTORS AND OFFICERS OF QUASI-BANKS AND TRUST ENTITIES

(Appendix to Sec. 4150Q)

RULE I – GENERAL PROVISIONS

Section 1. Title. – These Rules shall be known as the BSP Rules of Procedure on Administrative Cases Involving Directors and Officers of Quasi-Banks and Trust Entities.

Sec. 2. Applicability. – These Rules shall apply to administrative cases filed with or referred to the Office of Special Investigation (OSI), BSP, involving directors and officers of quasi-banks and trust entities pursuant to Section 37 of R.A. No. 7653 (The New Central Bank Act) and Sections 16 and 66 of R.A. No. 8791 (The General Banking Law of 2000).

The disqualification of directors and officers under Section 16 of R.A. No. 8791 shall continue to be covered by existing BSP rules and regulations.

Sec. 3. Nature of Proceedings. – The proceedings under these Rules shall be summary in nature and shall be conducted without necessarily adhering to the technical rules of procedure and evidence applicable to judicial trials. Proceedings under these Rules shall be confidential and shall not be subject to disclosure to third parties, except as may be provided under existing laws.

RULE II – COMPLAINT

Sec. 1. Complaint. - The complaint shall be in writing and subscribed and sworn to by the complainant. However, in cases initiated by the appropriate department of the BSP, the complaint need not be under oath. No anonymous complaint shall be entertained.

Sec. 2. Where to file. – The complaint shall be filed with or referred to the OSI.

Sec. 3. Contents of the Complaint - The complaint shall contain the ultimate facts of the case and shall include:

a. full name and address of the complainant;

b. full name and address of the person complained of;

c. specification of the charges;

d. statement of the material facts;

e. statement as to whether or not a similar complaint has been filed with the BSP or any other public office.

The complaint shall include copies of documents and affidavits of witnesses, if any, in support of the complaint.

RULE III – DETERMINATION OF *PRIMA FACIE* CASE AND PROSECUTION OF THE CASE

Sec. 1. Action on Complaint.- Upon determination that the complaint is sufficient in form and substance, the OSI shall furnish the respondent with a copy thereof and require respondent to file within ten (10) days from receipt thereof, a sworn answer, together with copies of documents and affidavits of witnesses, if any, copy furnished the complainant.

Failure of the respondent to file an answer within the prescribed period shall be considered a waiver and the case shall be deemed submitted for resolution.

Sec. 2. Preliminary Investigation. – Upon receipt of the sworn answer of the respondent, the OSI shall determine whether there is a *prima facie* case against the respondent. If a *prima facie* is

established during the preliminary investigation, the OSI shall file the formal charge with the Supervised Banks Complaints Evaluation Group (SBCEG), BSP. However, in the absence of a *prima facie* case, the OSI shall dismiss the complaint without prejudice or take appropriate action as may be warranted.

Sec. 3. Formal Charge. – The formal charge shall contain the name of the respondent, a brief statement of material or relevant facts, the specific charge, and the pertinent provisions of banking laws, rules or regulations violated.

Sec. 4. Prosecution. – The OSI shall prosecute the case. The complainant may be assisted or represented by counsel, who may be deputized for such purpose, under the direction and control of the OSI.

RULE IV – PROCEEDING BEFORE THE HEARING PANEL OR HEARING OFFICER

Sec. 1. Filing of the Formal Charge.- The OSI shall file the formal charge before the SBCEG. It shall also furnish the SBCEG with supporting documents relevant to the formal charge.

Sec. 2. Hearing Officer and Composition of the Hearing Panel. – The case shall be heard either by a Hearing Officer or a Hearing Panel, which shall be composed of a Chairman and two (2) members, all of whom shall be designated by the SBCEG. The SBCEG shall determine whether the case shall be heard either by a Hearing Panel or a Hearing Officer.

Sec. 3. Answer. – The Hearing Panel or Hearing Officer shall furnish the respondent with a copy of the formal charge, with supporting documents relevant thereto, and shall require him to submit, within ten (10) days from receipt thereof, a sworn answer, copy of which shall be furnished the prosecution.

The respondent, in his answer, shall specifically admit or deny all the charges specified in the formal charge, including the attachments. Failure of the respondent to comment, under oath, on the documents attached thereto shall be deemed an admission of the genuineness and due execution of said documents.

Sec. 4. Waiver. – In the event that the respondent, despite due notice, fails to submit an answer within the prescribed period, he shall be deemed to have waived his right to present evidence. The Hearing Panel or Hearing Officer shall issue an Order to that effect and direct the prosecution to present evidence *ex parte*. Thereafter, the Hearing Panel or Hearing Officer shall submit a report on the basis of available evidence.

Sec. 5. Preliminary Conference.– Upon receipt of the answer of respondent, the Hearing Panel or Hearing Officer shall set the case for preliminary conference for the parties to consider and agree on the admission or stipulation of facts and of documents, simplification of issues, identification and marking of evidence and such other matters as may aid in the prompt and just resolution of the case. Any evidence not presented and identified during the preliminary conference shall not be admitted in subsequent proceedings.

Sec. 6. Submission of Position Papers.– After the preliminary conference, the Hearing Panel or Hearing Officer shall issue an Order stating therein the matters taken up, admissions made by the parties and issues for resolution. The Order shall also direct the parties to simultaneously

submit, within ten (10) days from the receipt of said Order, their respective position papers which shall be limited to a discussion of the issues as defined in the Order.

Sec. 7. Hearing. – After the submission by the parties of their position papers, the Hearing Panel or Hearing Officer shall determine whether or not there is a need for a hearing for the purpose of cross-examination of the affiant(s). If the Hearing Panel or Hearing Officer finds no necessity for conducting a hearing, he shall issue an Order to the effect.

In cases where the Hearing Panel or Hearing Officer deems it necessary to allow the parties to conduct cross-examination, the case shall be set for hearing. The affidavits of the parties and their witnesses shall take the place of their direct testimony.

RULE V – PROHIBITED MOTIONS

Sec. 1. Prohibited Motions. – No motion to dismiss or quash, motion for bill of particulars and such other dilatory motions shall be allowed in the cases covered by these Rules.

RULE VI – RESOLUTION OF THE CASE

Sec. 1. Contents and Period for Submission of Report. – Within sixty (60) days after the Hearing Panel or Hearing Officer has issued an Order declaring that the case is submitted for resolution, a report shall be submitted to the Monetary Board. The report of the Hearing Panel or Hearing Officer shall contain clearly and distinctly the findings of facts and conclusions of law on which it is based.

Sec. 2. Rendition and Notice of Resolution. – After consideration of the report, the Monetary Board shall act thereon and cause true copies of its Resolution to be served upon the parties.

Sec. 3. Finality of the Resolution.– The Resolution of the Monetary Board shall become final after the expiration of fifteen (15) days from receipt thereof by the parties, unless a motion for reconsideration shall have been timely filed.

Sec. 4. Motion for Reconsideration.– A motion for reconsideration may only be entertained if filed within fifteen (15) days from receipt of the Resolution by the parties. No second motion for reconsideration shall be allowed.

RULE VII – APPEAL

Sec. 1. Appeal. – An appeal from the Resolution of the Monetary Board may be taken to the Court of Appeals within the period and in the manner provided under Rule 43 of the Revised Rules of Court.

RULE VIII – EXECUTION OF RESOLUTION

Sec. 1. Resolution Becoming Executory. – The Resolution of the Monetary Board shall become executory upon the lapse of fifteen (15) days from receipt thereof by the parties or from the receipt of the denial of the motion for reconsideration.

Sec. 2. Effect of Appeal. – The appeal shall not stay the Resolution sought to be reviewed unless the Court of Appeals shall direct otherwise upon such terms as it may deem just.

Sec. 3. Enforcement of Resolution.– When the Resolution orders the imposition of fines, suspension or removal from office of respondent, the

enforcement thereof shall be referred to the appropriate department of the BSP.

RULE IX – MISCELLANEOUS PROVISIONS

Section 1. Repeal. – All existing rules, regulations, orders or circulars or any part thereof inconsistent with these Rules are hereby repealed, amended or modified accordingly.

Section 2. Separability Clause. – If any part of these Rules is declared unconstitutional or illegal, the other parts or provisions shall remain valid.

FORMAT CERTIFICATION

[Appendix to Subsec. 4235Q.12 (2008 - 4211Q.12)]

_____
Name of Bank

CERTIFICATION

Pursuant to the requirements of Subsec. 4235Q.12, I HEREBY CERTIFY that on all banking days of the semester ended _____ that the _____ (quasi-bank) did not enter into any repurchase agreement covering government securities, commercial papers and other negotiable and non-negotiable securities or instruments that are not documented in accordance with existing BSP regulations and that it has strictly complied with the pertinent rules of the SEC and the BSP on the proper sale of securities to the public and performed the necessary representations and disclosures on the securities particularly the following:

1. Informed and explained to the client all the basic features of the security being sold on a without recourse basis, such as, but not limited to:

   a. Issuer and its financial condition;
   b. Term and maturity date;
   c. Applicable interest rate and its computation;
   d. Tax features (whether taxable, tax paid or tax-exempt);
   e. Risk factors and investment considerations;
   f. Liquidity feature of the instrument:

   f.1. Procedures for selling the security in the secondary market (e.g., OTC or exchange);
   f.2. Authorized selling agents; and
   f.3. Minimum selling lots.

   g. Disposition of the security

   g.1. Registry (address and contact numbers)
   g.2. Functions of the registry
   g.3. Pertinent registry rules and procedures

   h. Collecting and Paying Agent of the principal and interest

   i. Other pertinent terms and conditions of the security and if possible, a copy of the prospectus or information sheet of the security.

2. Informed the client that pursuant to BSP Circular No. 392 dated 23 July 2003 –

   • Securities sold under repurchase agreements shall be physically delivered, if certificated, to a BSP-accredited custodian that is mutually acceptable to the client and the quasi-bank, or by means of book-entry transfer to the appropriate securities account of the BSP-accredited custodian in a registry for said securities, if immobilized or dematerialized, and

- Securities sold on a without recourse basis are required to be delivered physically to the purchaser, or to his designated custodian duly accredited by the BSP, if certificated, or by means of book-entry transfer to the appropriate securities account of the purchaser or his designated custodian in a registry for said securities if immobilized or dematerialized

3. Clearly stated to the client that:

   a. The quasi-bank does not guarantee the payment of the security sold on a "without recourse basis" and in the event of default by the issuer, the sole credit risk shall be borne by the client; and

   b. The quasi-bank is not performing any advisory or fiduciary function.

_____
Name of Officer
Position

Date _____

SUBSCRIBED AND SWORN to before me, this _____ day of _____, affiant exhibiting his Community Tax Certificate as indicated below:

Name	Community Tax Cert. No.	Date/Place Issued

Notary Public

Annex Q-36-a

FORMAT CERTIFICATION
(Annex to Appendix Q-36)

_____
Name of Bank

CERTIFICATION

Pursuant to the requirements of Subsec 4235Q.12, I hereby certify that as of 31 January 2005, the _____ (name of quasi-bank) does not have any outstanding repurchase agreements covering government securities, commercial papers and other negotiable and non-negotiable securities or instruments that are not documented in accordance with existing BSP regulations.

_____
Name of Officer
Position

SUBSCRIBED AND SWORN to before me, this _____ day of _____, affiant exhibiting his Community Tax Certificate as indicated below:

Name	Community Tax Cert. No.	Date/Place Issued

Notary Public

DUTIES AND RESPONSIBILITIES OF BANKS AND THEIR DIRECTORS/OFFICERS IN ALL CASES OF OUTSOURCING OF BANKING FUNCTIONS

[Appendix to Sec. 4162Q (2008 - 4192Q), 4190S, 4190P and 4190N]

a. *When outsourcing of banking functions is allowed by law, banks shall:*

(1) Carry out the same in accordance with proper standards, ensuring the integrity of the data, systems and controls of the banks and subject to the supervisory, regulatory and administrative authority of the BSP over the banks and their directors/officers;

(2) Be responsible for the performance thereof in the same manner and to the same extent as it was before the outsourcing;

(3) Comply with all laws and regulations governing the quasi-banking activities/services performed by the qualified service providers in its behalf such as, but not limited to, keeping of records and preparation of reports, signing authorities, internal control and clearing regulations; and

(4) Manage, monitor and review on an ongoing basis the performance by the qualified service providers of the outsourced banking activities/services.

b. *Prohibition against outsourcing certain banking functions*. No bank or any director, officer, employee, or agent thereof shall outsource inherent banking functions.

For purposes of this Section, *outsourcing of inherent banking functions* shall refer to any contract between the bank and a service provider for the latter to supply, or any act whereby the latter supplies, the manpower to service the deposit substitute transactions of the former.

Banks cannot outsource management functions except as may be authorized by the Monetary Board when circumstances justify.

c. *Outsourcing of information technology systems/processes*. Subject to prior approval of the Monetary Board, banks may outsource all information technology systems and processes except for functions excluded in Item *"1"*.

(1) Certain functions affecting the ability of the bank to ensure the fit of technology services deployed to meet its strategic and business objectives and to comply with all pertinent banking laws and regulations, such as, but not limited to, strategic planning for the use of information technology; determination of system functionalities; change management inclusive of quality assurance and testing; service level and contract management; and security policy and administration, may not be outsourced. Subject to prior approval of the Monetary Board and submission of the same documentary requirements in Item *"(2)"* hereof, consultants and/or service providers may be engaged to provide assistance/ support to the bank personnel assigned to perform such functions.

(2) *Documentary requirements*. A bank intending to outsource information technology systems and processes shall submit the following documents to BSP which shall treat the same as strictly confidential:

(a) Proposed contract between the bank and the service provider which should, at a minimum, include all the following:

(i) Complete description of the work to be performed or services to be provided;

(ii) Fee structure;

(iii) Provisions regarding on-line communication availability, transmission line security, and transaction authentication;

(iv) Responsibilities regarding hardware, software and infrastructure upgrades;

(v) Provisions governing amendment and pre-termination of contract;

(vi) Mandatory notification by the service provider of all systems changes that will affect the bank;

(vii) Details of all security procedures and standards;

(viii) Responsibility, fines, penalties and accountability of the service provider for errors, omissions and frauds;

(ix) Confidentiality clause covering all data and information; solidary liability of service provider and bank for any violation of R.A. No. 1405 (Bank Deposits Secrecy Law) actions that the bank may take against the service provider for breach of confidentiality or any form of disclosure of confidential information; and the applicable penalties;

(x) Segregation of the data of the bank from that of the service provider and its other clients;

(xi) Disaster recovery/business continuity contingency plans and procedures;

(xii) Adequate insurance for fidelity and fire liability;

(xiii) Ownership/maintenance of the computer hardware, software (program source code), user and system documentation, master and transaction data files;

(xiv) Guarantee that the service provider will provide necessary levels of transition assistance if the bank decides to convert to other service providers or other arrangements;

(xv) Access to the financial information of the service provider;

(xvi) Access of internal and external auditors to information regarding the outsourced activities/services which they need to fulfill their respective responsibilities;

(xvii) Access of BSP to the operations of the service provider in order to review the same in relation to the outsourced activities/services;

(xviii) Provision which requires the service provider to immediately take the necessary corrective measures to satisfy the findings and recommendations of BSP examiners and those of the internal and/or external auditors of the bank and/or the service provider; and

(xix) Remedies for the bank in the event of change of ownership, assignment, attachment of assets, insolvency, or receivership of the service provider.

(b) Minutes of meetings of the board of directors of the bank concerned signed by majority thereof, certified by the secretary and attested by the president documenting their discussions on the following:

(i) The benefits and advantages of outsourcing with respect to, among others, its role and contribution to the accomplishment of the strategic and business plans of the bank as well as the economy, efficiency and quality of its over-all operations;

(ii) The careful and diligent evaluation, prior to selecting the service provider with which it is entering into an outsourcing contract, by the bank of various service providers and their proposals, including their reputation, financial condition, cost for development, maintenance and support, internal controls, recovery processes, service level agreements, availability of competent, technically qualified and experienced personnel, strategic or convenient location of support services and such similar other considerations;

(iii) The creation, organization and membership of a senior management oversight committee to handle and oversee the efficient implementation and monitoring of the applications/

operations of the service provider to ensure that the same is in accordance with the existing information technology initiatives, policies and guidelines of the bank; the list of the members of such committee, its organizational chart, and a detailed description of the roles and responsibilities of its members must be included in the minutes of the meeting or submitted as attachments thereto;

(iv) The creation, organization and membership of a help desk to resolve all queries, problems and other concerns arising from the applications/operations rendered by the service provider; and

(v) The systems and user acceptance tests that will be conducted by the service provider before full implementation of the outsourced systems/processes and the unsatisfactory results of which shall be valid ground to rescind the contract with the service provider.

(c) Profile of the selected service provider or the non-bank partner, in case of joint ventures and other similar arrangements, which should include:

(i) Most recent and complete financial and operational information;

(ii) Track record;

(iii) List of clientele, particularly banks and the services provided thereto by the service provider; and

(iv) At the option of the service provider or non-bank partner, other documents demonstrative of its competence and reputation in the field of information technology as applied to banking operations.

d. *Outsourcing of other banking functions*

(1) Subject to prior approval of the Monetary Board, banks may outsource the following functions, services or activities:

(a) data imaging, storage, retrieval and other related systems;

(b) clearing and processing of checks not included in the PCHC System;

(c) printing of bank deposit statements;

(d) credit card services;

(e) credit investigation and collection;

(f) processing of export, import and other trading transactions;

(g) property appraisal;

(h) property management services;

(i) internal audit, subject to the following conditions:

(i) the board of directors and senior management of the regulated entity remain responsible for maintaining an effective system of internal control and for providing active oversight of the outsourced internal audit activities/ functions;

(ii) the external service provider shall be an independent external auditor included in the list of BSP-selected external auditors or a parent company which owns or controls more than fifty percent (50%) of the subscribed capital stock of the outsourcing entity: *Provided*, That Item *"A2"* of the general requirements under *Appendix Q-30* shall apply to the parent company while Items *"A2"*, *"A4"*, *"A5"*, and *"A6"* shall apply to the independent external auditor;

(iii) the contract/service agreement with the external service provider shall not be entered into for a period longer than five (5) years;

(iv) there shall be a contingency plan to mitigate any significant disruption, discontinuity or gap in audit coverage, particularly for high-risk areas;

(v) the written engagement contract or service agreement with the external service provider shall, as a minimum:

(aa) define the rights, expectations and responsibilities of both parties;

(bb) set the scope and frequency of, and the fees to be paid for, the work to be performed by the external service provider;

(cc) state that the outsourced internal audit services are subject to regulatory

review and that BSP examiners shall be granted full and timely access to internal audit reports and related working papers;

(dd) state that the external service provider will not perform management functions, make management decisions, or act or appear to act in a capacity equivalent to that of a member of management or an employee of the institution, and will comply with professional and regulatory independence guidelines;

(ee) specify that the external service provider must maintain the audit reports and related working papers/files for at least five (5) years;

(ff) state that internal audit reports are the property of the institution, that the institution will be provided with copies of related working papers/files it deems necessary, and any information pertaining to the institution must be kept confidential; and

(gg) establish a protocol for changing the terms of the service contract and stipulations for default and termination of the contract;

(j) marketing loans, deposits and other bank products and services, provided it does not involve the actual opening of deposit accounts;

(k) general bookkeeping and accounting services: *Provided*, That these activities do not include servicing bank deposits or other inherent banking functions;

(l) offsite records storage services;

(m) front/back office functions, i.e., trade support services and downstream processing activities, by parent to a subsidiary or vice-versa, subject to the following conditions:

(i) The bank intending to outsource the aforementioned functions shall certify that the front office functions to be done by its parent/subsidiary (service provider) shall be limited to trade support services;

(ii) The bank shall remain a parent/ subsidiary of its subsidiary/parent (service provider) and such service provider shall service only entities belonging to its business group;

(iii) The bank shall certify that no inherent quasi-banking functions involving deposit substitute transactions shall be outsourced to its parent/subsidiary (service provider);

(iv) The bank shall submit a Service Level Agreement duly signed by the concerned parties and any amendments thereto, detailing the functions to be outsourced, the respective responsibilities of the bank and its parent/subsidiary (service provider), and a confidentiality clause; and

(v) Any breach in any of the above conditions shall subject the outsourcing of the aforementioned banking functions to all the requirements of this Appendix;

(n) back up and data recovery operations;

(o) Call center operations for credit card and bank services provided that such bank services do not involve inherent banking functions;

(p) loans processing, credit administration and documentation services in favor of subsidiaries, affiliates and other companies related to it by at least five percent (5%) common ownership;

(q) loan documentation services (such as mortgage registration); and

(r) such other activities as may be determined by the Monetary Board.

(2) Without need of prior Monetary Board approval, banks may outsource the following functions, services or activities:

(a) printing of loan statements and other non-deposit records, forms and promotional materials;

(b) transfer agent services for debt and equity securities;

(c) messenger, courier and postal services;

(d) security guard services;

(e) vehicle service contracts;

(f) janitorial services;

(g) public relations services, procurement services, and temporary staffing: *Provided*, That these activities do not include servicing bank deposit substitutes or other inherent banking functions;

(h) sorting and bagging of notes and coins;

(i) maintenance of computer hardware, e.g., disk drives, printers, monitors, UPS, network cabling systems;

(j) payroll of employees;

(k) telephone operator/receptionist services;

(l) sale/disposal of acquired assets (ROPA);

(m) human-resource related services (such as personnel training and development, background investigation and salary benchmarking service)

(n) buildings, ground and other facilities maintenance;

(o) legal services from local legal counsel;

(p) compliance risk assessment and testing;

(q) tax compliance services; *Provided,* That the service provider is not also the external auditor of the bank;

(r) ATM card plastic embossing service, subject to the following conditions:

(i) Only the ATM card number and the name of the depositor are printed/ indicated on the plastic card and stored in the magstripe; and

(ii) Account/Transaction validation is done at the host level,i.e., the bank's computer, as the card number stored in the magstripe is linked to the deposit account number residing at the same host computer;

(s) ATM incident management service; *Provided*, That the messages transmitted by the ATM machines to the service provider's monitoring system are purely ATM statuses and in no way shall client or transaction information be sent; and

(t) such other activities as may be determined by the Monetary Board.

e. *Service providers*. When allowed by law, banks may enter into outsourcing contracts only with service providers with demonstrable technical and financial capability commensurate to the services to be rendered.

f. *Review of subsisting outsourcing contracts*. Within six (6) months from 19 July 2005 –

(1) banks should submit a list of all their existing contracts with service providers, detailing the:

(a) services/activities being outsourced;

(b) terms of the contracts;

(c) measures, if any, undertaken by the bank and/or service provider to ensure the secrecy and confidentiality of all other data and information; and

(d) such other information as may be necessary to show compliance with the pertinent provisions of this Appendix or be required by the Monetary Board; and

(2) for outsourcing contracts not in accordance with this Appendix, the following alternative courses of action are available to the bank concerned:

(a) preterminate said contracts;

(b) renegotiate or remedy the same and submit the amendments thereto or new contracts to the BSP; or

(c) submit a program of compliance to the BSP.

(As amended by Circular Nos. 642 dated 30 January 2009, 623 dated 09 October 2008, 621 dated 16 September 2008, 610 dated 26 May 2008, 596 dated 11 January 2008, 548 dated 25 September 2006 and 543 dated 08 September 2006)

IMPLEMENTATION OF THE DELIVERY BY THE SELLER OF SECURITIES TO THE BUYER OR TO HIS DESIGNATED THIRD PARTY CUSTODIAN

[Appendix to Secs. 4441Q and 4144N and Subsecs. 4101Q.4, 4235Q.5 (2008 - 4211Q.4) and 4103N.3]

Section 1. Statement of Policy. Pursuant to the policy of the BSP to promote the protection of investors in order to gain their confidence in the securities market as enunciated under Circular Nos. 392 and 428 dated 23 July 2003 and 27 April 2004, respectively, the following rules/guidelines shall be observed by banks and NBFI under BSP supervision in their dealings in securities whether they are acting as seller, buyer, agent or custodian.

The disposition of compliance issues of this Appendix is shown in *Appendix Q-38a*.

The guidelines on the delivery of government securities by the selling bank to an investor's Principal Securities Account with the RoSS through the Client Interface System facility are in A*ppendix Q-38b*.

Sec. 2. Distinction Between a Custodian and a Registry. A securities custodian is a BSP-accredited bank or NBFI designated by the investor to perform the functions of safekeeping, holding title to the securities either in a nominee or trustee capacity, reports rendition, mark-to-market valuation, administration of dividends or interest earnings and representation of clients in corporate actions. It may also perform value added services such as collecting and paying and securities borrowing and lending as agent. A BSP-accredited custodian is considered a third party if it has no subsidiary or affiliate relationship with the issuer or seller of securities.

On the other hand, a securities registry, other than the BTr, is a BSP-accredited bank or NBFI designated or appointed by the issuer to maintain the securities registry book either in electronic or in printed form. It records the initial issuance of the securities and subsequent transfer of ownership and issues registry confirmation to the buyers/holders. Except as otherwise provided in existing BSP regulations, a BSP-accredited securities registry is considered a third party if it has no subsidiary or affiliate relationship with the issuer of securities.

Sec. 3. Registry of Scripless Securities of the Bureau of Treasury. The BTr, as operator of the RoSS , which serves as the official registry for GS, is not subject to BSP accreditation and is exempted from the independence requirement under the existing BSP regulations.

Sec. 4. Delivery of Securities. Pursuant to existing BSP regulations, securities sold on a without recourse basis shall be delivered by the seller to the purchaser, or to his designated BSP-accredited custodian which must not be a subsidiary or affiliate of the issuer or seller.

Sec. 5. Mode of Delivery. If the securities sold are certificated, delivery shall be effected physically to the purchaser, or to his designated BSP-accredited custodian. The certificate must be transferred to and registered under the name of the purchaser and properly recorded in the registry book. On the other hand, delivery of immobilized or dematerialized securities shall be effected by means of book entry transfer to the appropriate securities account of either: (1) the purchaser in a registry of said securities; or (2) the purchaser's designated custodian in a registry of said securities.

Book-entry transfer to a sub-account for clients under the primary account of the seller will not be deemed compliant with this requirement. The delivery must be supported by a confirmation of book-entry transfer to be issued by the securities registry in case of name on registry or by a confirmation receipt to be issued by the custodian in case of delivery to the purchaser's designated custodian.

Sec. 6. Client Information. Selling or dealing banks shall inform their clients of the requirements under Secs. 3 and 4 above, together with the complete list of all BSP-accredited custodians. The selling or dealing bank or NBFI must inform their clients that the choice of custodian is the sole prerogative of the securities purchaser. The seller or dealer may, however, indicate to their clients their preferred custodian. Attached as Annex "A" is a suggested template of the letter to the client.

Sec. 7. Custodianship Agreement. The securities owner/purchaser shall enter into a custodianship agreement with a BSP-accredited third-party custodian of his choice. However, the securities purchasers/owners may designate/ appoint through a special power of attorney (SPA) a representative or agent for the purpose of opening and maintaining an account with the BSP-accredited third-party custodian: *Provided,* That if the securities seller or dealer is appointed as an agent, its authority shall be limited to the opening of the custodianship account and the execution of trade transactions (i.e. buying and selling instructions including relaying of instructions to the custodian to receive or deliver securities in order to consummate the buy/sell transactions). It shall be the responsibility of the custodian to protect the interest of the client by ensuring that the agent is acting within the scope of his authority.

Sec. 8. Authority of the Securities Owner/Purchaser to Revoke Special Power of Attorney. Whenever a securities owner/purchaser executes an SPA designating/appointing an agent to open and maintain a custodianship account with a BSP-accredited third party custodian pursuant to Sec. 6 above, said SPA shall clearly stipulate that the appointment of the agent is revocable at the instance of the securities owner/ purchaser or his agent. Any revocation by either party shall be made in writing and must be given to the other party and to the custodian. The custodian is hereby enjoined to acknowledge and respect said right of the client. It is, however, understood that the revocation of the SPA shall be without prejudice to any transaction executed by the agent or custodian prior to said party's knowledge of the revocation. Upon revocation of the SPA, the custodian shall deal directly with the securities owner or his newly appointed agent. However, the custodian has the right to impose additional reasonable conditions similar to those being imposed on separate custody accounts maintained directly by individual or corporate clients.

Sec.9. Reports of the Custodian. Periodic reports of the custodian on account balances shall be rendered at least quarterly and shall reflect the mark-to-market valuation of the security in accordance with existing BSP regulations. It shall be delivered, mailed or electronically transmitted directly to the securities owner unless the securities owner gives a written request or instruction directly to the custodian to deliver said reports to a person/entity named therein. Said request/ instruction of the securities owner shall

indicate that he is appointing an agent/ representative for the purpose, notwithstanding contrary advice of the BSP.

Aside from the periodic reports, the custodian shall also issue confirmation of transfers of ownership as they occur in either electronic or printed form delivered directly to the securities owner, unless the securities owner gives a written request or instruction directly to the custodian to deliver the confirmation reports to a person/entity named therein.

Sec. 10. Right of the Securities Owner to Sell his Securities. Subject to the requirements of existing laws and regulations, securities owners shall have the right to choose the best buyers of his securities in the secondary market, without limiting himself to the original selling or dealing bank that he transacted with. The securities seller or dealer shall not impose any condition that will impair this right of the securities owner or leave him no alternative except to sell his securities exclusively to the selling or dealing bank.

Sec. 11. Undelivered Securities. In cases where banks or NBFIs under BSP supervision maintain custody of securities which were sold prior to the effectivity of Circular No. 457 dated 14 October 2004 to clients who are unable or unwilling to take delivery of said securities pursuant to the provisions of Circular No. 392 dated 23 July 2003 but who declined to deliver their existing securities to a BSP-accredited third party custodian, said banks/financial institutions shall:

a. report on a quarterly basis to the appropriate department of the SES the volume of said securities broken down into maturity dates, type of security, ISIN or applicable certificate or reference number, and registry; and

b. ensure that said securities under custody are segregated from their proprietary holdings.

Sec. 12. Compliance with the Anti-Money Laundering Act of 2001. For purposes of compliance with the requirements of R.A. No. 9160, otherwise known as the "Anti-Money Laundering Act of 2001" regarding customer identification, recordkeeping and reporting of suspicious transactions, a BSP-accredited custodian may rely on referral by the seller/issuer of securities, in lieu of the face-to-face contact with client, subject to the following conditions:

a. the seller/issuer is also a covered institution;

b. the seller/issuer certifies to the custodian that it has performed its own KYC screening on the client;

c. the custodian has unchallenged access to the KYC records/documents of the referring seller/issuer pertaining to the referral client;

d. the custodian maintains a record of the referral together with the minimum information/documents required under the law and its implementing rules and regulations; and

e. the seller/issuer must provide the custodian with the following minimum information/documents:

For individual clients:

1. Name;
2. Present address;
3. Permanent address;
4. Date and place of birth;
5. Nationality;
6. Nature of work and name of employer or nature of self-employment/ business;
7. Contact numbers;
8. TIN, SSS number or GSIS number;
9. Specimen signature; and
10. Source of fund(s);

For corporate clients:

1. Articles of Incorporation/Partnership;
2. By-laws;
3. Official address or principal business address;
4. List of directors/partners;
5. List of principal stockholders owning at least two percent (2%) of the capital stock;
6. Contact numbers;
7. Beneficial owners, if any;
8. Authorized signatories;
9. Board/Partnership Resolution on the authority of the signatories; and
10. Verification of the identification and authority of the person purporting to act on behalf of the client.

Sec. 13. Safekeeping of Customers' Identification Documents. The BSP accredited third-party custodian may entrust to the referring seller/dealer the safekeeping and maintenance of the customer identification documents supporting its KYC certification: *Provided,* That:

a. The BSP accredited custodian has received a certification from the seller/dealer that it has in its possession all required KYC documents and the custodian shall maintain a list of such documents;

b. The accredited custodian shall have unhampered access to the KYC documents for its own verification; and

c. KYC or customer identification documents shall be made available to regulators for verification upon request.

Nothwithstanding Secs. 12 and 13, the custodian is not precluded from conducting its own KYC activities and maintaining direct custody of the KYC documents of its clients.

(Circular No. 524 dated 31 March 2006, as amended by M-2007-002 dated 23 January 2007)

Annex A

TEMPLATE OF LETTER TO INVESTOR

Dear Investor:

We wish to inform you that the Bangko Sentral ng Pilipinas (BSP), in July of 2003 issued **Circular No. 392, Series of 2003,** which requires all securities sold by banks on a **"without recourse basis"** (i.e. the bank has no liability to the buyer of securities in paying the obligation due on the security) to be delivered to the buyer/purchaser of securities through any of the following means:

(a) **If the security is evidenced by a certificate of indebtedness**, the certificate must be transferred in the name of the purchaser/buyer and physically delivered to the purchaser/buyer or to his designated BSP-accredited third party custodian.

(b) **If the security is immobilized or dematerialized** (i.e., that the security is not evidenced by a certificate of indebtedness and instead security account is created in the electronic books of the registry in the name of the purchaser/buyer or his designated custodian):

i. The security must be delivered by book-entry transfer to the appropriate securities account of the buyer in the registry of said securities which must be evidenced by a confirmation in writing by the registrar to the buyer. The confirmation of sale or document of conveyance shall be physically delivered by the seller or dealer to the buyer, or

ii. The security must be delivered by book-entry transfer to the appropriate securities account of the BSP-accredited third party custodian designated by the buyer/purchaser in the registry of said securities which must be evidenced by a confirmation in writing by the registrar to the said BSP-accredited third party custodian, who shall in turn issue to the securities owner a delivery receipt acknowledging receipt of the securities

Circular No. 392 is part of a package of reforms to support the development of the domestic capital market through enhanced investor protection and greater market transparency. It provides for a more defined role and responsibilities for the custodians and registrars and a stricter supervision and regulation thereof by the BSP. It aims to provide the client with the following benefits:

a. Full control and possession of the securities purchased;
b. Independent validation of the existence of securities purchased;
c. Regular reporting of securities holdings; and
d. Capability to choose most competitive counter-parties in case of sale, pledge, transfer, and lending of securities.

Moreover, Circular No. 392, which amends CBP Circular 437-74, seeks to address the changes in the legal framework brought by the developments in the market, i.e. where purchase of securities may be evidenced not only by transfer of certificates but also by electronic book-entry transfer of ownership in the books of the registrar for said security.

As an investor, therefore, of securities which is dematerialized or scripless, you have **the option** to require your dealer/broker to deliver the securities to you by requiring them to have the securities registered directly in **your name in the registry** of said securities **or** by requiring them to have the securities registered in the name of the BSP **accredited third party custodian** of your choice who in turn will credit your securities account with them.

The **registry** is a BSP-accredited bank or non-bank financial institution (NBFI) designated or appointed by the Issuer to (1) maintain the securities registry book; (2) record the (a) issuance of the securities and (b) subsequent transfers of ownership thereof; and (3) issue registry confirmation to the buyers/holders of security.

The **custodian**, on the other hand, is a BSP-accredited bank or NBFI designated by the investor to safekeep the security by allowing it to hold title to the security, either in a nominee or trustee capacity, to enable it to perform the following administrative functions/ services related to investing in a security or various securities: (i) Mark to market valuation of security that will enable the client to know the value of his investment at any period in time; (ii) compute and collect the interest due on the security; (iii) render statements on outstanding securities under safekeeping; (iv) represents the client (per its instruction) in the events of default or breach of contract of the issuer; and (v) lend the security of the clients as "agent" that will enable the client to earn additional income on the security.

The registrars and custodians underwent a rigorous evaluation process by the BSP to determine whether they have the following: (i) adequate capital to cover for potential operating risks related to performing its custody functions; (ii) competent management team to manage the company with responsibility and proper corporate ethics; (iii) robust technology system to operate the custody business efficiently; and (iv) favorable track record or significant experience in the custody business or related business. They will also undergo regular audit by the BSP to ensure that they comply with BSP rules and regulations and will be subject to penalties and administrative sanctions for any violation thereof.

As of date, BSP has accredited the following registrars and custodians: Bank of the Philippine Islands, CITIBANK N.A., Deutsche Bank, Hongkong and Shanghai Banking Corporation, Philippine Depository and Trust Corporation, and Standard Chartered Bank.

The Registry of Scripless Securities (RoSS) operated by the Bureau of Treasury (BTR) which is acting as a registry for government securities, is automatically accredited as securities registry. However, the BTR, as registry, cannot act as custodian of government securities pursuant to the opinion of the Secretary of Justice rendered on 17 January 2005 due to irreconcilable conflict of loyalties that is anathema to agency if the same institution were to act as registrar and custodian at the same time.

The custodian shall render periodic reports on your account balances on a quarterly basis, or at such interval as you may require. Moreover, the custodian shall issue to you a confirmation of any transfer of ownership as it occurs, in either electronic or printed forms. Said reports shall be delivered/mailed directly at your address unless you give a written instruction directly to the custodian to deliver the said reports to your designated person/ entity. You are, however, required to acknowledge in the written instruction that you are designating another person/entity to receive the periodic reports from the custodian, notwithstanding contrary advice of the BSP.

Please note that the abovementioned arrangements may change once the BSP issues more detailed implementing rules and guidelines to the abovementioned circulars. We will update you if and when these developments occur.

Please fill up and sign the required documentation of your chosen custodian and we will forward the same to them so that your securities account can be opened as soon as possible. You may, however, designate/appoint an agent for this purpose. In either case, the custody arrangement may or may not entail additional fees.

If you have any further questions, please call us so that we can refer the matter to the appropriate custodian/registrar.

Very truly yours,

(Circular No. 524 dated 31 March 2006, as amended by M-2007-002 dated 23 January 2007)

DISPOSITION OF COMPLIANCE ISSUES ON APPENDIX Q-38

[Appendix to Secs. 4441Q and 4144N and Subsecs. 4101Q.4, 4235Q.5 (2008 - 4211Q.4) and 4103N.3]

A. The Monetary Board, in its Resolution No. 581 dated 05 May 2006 approved a thirty (30) calendar day period from 05 June 2006 within which banks/non-banks will effect revisions to non-conforming SPAs issued by investor-clients to strictly conform to the limited authority provisions of Section 7 of *Appendix Q-38*, subject to the following conditions:

1. The clean-up of SPAs will cover those issued by clients prior to Circular No. 524 dated 31 March 2006;

2. Custodians will allow transfers of securities from proprietary accounts of dealers to their omnibus principal custody accounts within the period;

3. There will be no penalties imposed for dealer-banks and accredited securities custodians that allowed non-compliant SPAs prior to Circular No. 524 dated 31 March 2006 or those issued under Circular Letter dated 4 August 2005 if corrected within the thirty (30)-day period; and

4. Non-compliance with other provisions of *Appendix Q-38* are not covered/qualified to be corrected within the thirty (30)-day period and are therefore subject to the usual penalty/ sanctions under existing regulations.

B. The Monetary Board, in its Resolution No. 876 dated 06 July 2006 approved the following disposition of compliance issues for the period of 05 July 2006 - 04 August 2006:

1. The sending by a dealing bank to all its clients of:

(a) a notice indicating a limitation on the authority of the dealing bank pursuant to Section 7 of *Appendix Q-38*; and

(b) compliant SPA for execution will be deemed substantial compliance only as of 05 July 2006. Proof thereof should be preserved for examination purposes.

2. Custodians will be deemed in substantial compliance as of 05 July 2006 if they have obtained confirmation from the dealing banks that notifications on the limitation of the dealing bank's authority, together with a compliant SPA for the clients' signature, have been sent to all their clients. Absent confirmation from the dealing bank of the sending of notices and the revised SPA, the custodian should immediately freeze (i.e., no new movements in the security, except sale or disposition thereof) the account to be considered in substantial compliance.

3. Absent a compliant SPA, the dealing bank and custodian should "freeze" the account of the client. Accordingly, if a client wants to transact with securities, the dealing bank must require the submission of an executed compliant SPA before any new transaction can be entered into. Otherwise, the dealing bank will be subject to the appropriate penalties prescribed under Subsec. X441.29. However, for the period of 05 July 2006 - 04 August 2006, transactions by the dealing bank with its clients, absent a compliant SPA but to which an advice on the limitation of the authority of the dealing bank and a compliant SPA for signature have been sent, will be subject to a fine of ₱10,000.00 per transaction/day: *Provided,* That the total penalty arising from that class of violation for the said period shall not exceed ₱100,000.00, computed in accordance with Section 37 of Republic Act No. 7653 (The New Central Bank Act). Furthermore, the Custodian will not be subject to any penalties for accepting securities subject of the transaction.

4. Starting on 05 August 2006, the penalties under Subsec. X441.29 shall be applied for any violation of the provisions of *Appendix Q-38*. Custodians shall be required to freeze the securities account for those without a compliant SPA from the investor.

(M-2006-009 dated 18 July 2006 and M-2006-002 dated 05 June 2006)

DELIVERY OF GOVERNMENT SECURITIES TO THE INVESTOR'S PRINCIPAL SECURITIES ACCOUNT WITH THE REGISTRY OF SCRIPLESS SECURITIES

[Appendix to Secs. 4441Q and 4144N, Subsecs. 4101Q.4, 4235Q.5 (2008 - 4211Q.4) 4103N.3, and 4103N.4]

The following are the guidelines on the delivery of government securities by the selling QB and/or NBFI under the supervision of the BSP to an investor's Principal Securities Account with the RoSS through the Client Interface System facility as compliance with the requirement of effective delivery under Secs. 4441Q and 4144N, Subsecs. 4101Q.4, 4101Q.5, 4235Q.5, 4103N.3 and 4103N.4:

(a) QBs/NBFIs, acting either as an accredited GSEDs or licensed government securities dealers, shall execute the attached Memorandum of Agreement (MOA) with the BTr regarding the creation of the Principal Securities Account with the RoSS on or before 31 January 2007. The MOA between the BTr and GSED is attached as Annex A.

(b) If the dealing QB/NBFI is designated as the agent of the client/investor, the authority of the dealing QB/NBFI under the SPA executed by the client/investor shall be limited to the opening of the Principal Securities Account with the RoSS and the execution of trade transactions (i.e., buying and selling instructions, including relaying of instructions to the BTr, as operator of the RoSS, to receive and deliver securities in order to consummate the buy/sell transaction).

(c) QBs/NBFIs shall require their clients/investors who have manifested the desire to have their own Principal Securities Account with the RoSS to execute (1) an SPA pursuant to Secs. 4441Q and 4144N, Subsecs. 4101Q.4, 4235Q.5, 4103N.3 and 4103N.4 and (2) the revised Investor's Undertaking (attached as Annex B) on or before 28 February 2007.

(d) Absent a compliant Investor's Undertaking and SPA as of 01 March 2007, the dealing QB/NBFI should freeze the account of the client/investor (i.e., no new movements in the account, except sale/ disposition upon written instruction by the client/investor): *Provided*, That starting 01 March 2007 no new Investors Principal Securities Account shall be created unless the investor submits a compliant Investor's Undertaking and SPA. Otherwise, the dealing QB/NBFI will be subject to the appropriate penalties prescribed under Secs. 4441Q and 4144N, and, Subsecs. 4101Q.4, 4101Q.5, 4235Q.5, 4103N.3, and 4103N.4.

(e) The sub-accounts in the RoSS maintained by dealing QBs/NBFI for their client/investor who either (1) declined in writing the delivery of his/its securities to a direct registry account under his/its name or a third-party custodian or (2) have not responded to the dealer's letter to the client/ investor as regards the disposition of his/its securities shall be frozen. However, sale/ disposition of securities in the sub-accounts shall be allowed upon written instruction by the client/investor to dispose the same: *Provided,* That in case of a client/ investor who as of 04 November 2004 has not responded to the dealer's letter regarding the disposition of his/its securities, the dealer should be able to obtain from the said client/investor the written instruction regarding the client/ investor's inability to take delivery of existing securities. For clarity, the sub-accounts maintained by the dealing QBs/ NBFIs shall not be considered a violation of Subsecs. 4101Q.4, 4235Q.5, 4103N.3 and 4104N.4: *Provided*, That (1) the same were created on or before 04 November 2004; and (2) no additional securities have been lodged thereon since 04 November 2004.

(M-2007-002 dated 23 January 2007)

Annex A

MEMORANDUM OF AGREEMENT

KNOW ALL MEN BY THESE PRESENTS:

This agreement made and entered into this _____ at _____, Philippines by and between:

The **BUREAU OF THE TREASURY**, a duly constituted government bureau under the Department of Finance, Republic of the Philippines, with principal office at Palacio del Gobernador Building, Gen. Luna corner A. Soriano Avenue, Intramuros, Manila, represented herein by the Treasurer of the Philippines, _____, and hereinafter referred to as "**BTr**";

-and-

_____, a domestic/ international/banking/financial institution organized and existing pursuant to the laws of the Republic of the Philippines/*(country of incorporation),* duly licensed by the Securities and Exchange Commission (SEC) to deal in securities, represented herein by _____ in her/his capacity as _____, and hereinafter referred to as the **Dealer**;

(the "BTr" and the "Dealer" may be referred to as a "Party" in the singular tense, as "Parties" in the plural/collective tense)

WITNESSETH: THAT

WHEREAS, the Registry of Scripless Securities (RoSS) is the official registry of government securities issued by the National Government through the BTr;

WHEREAS, the RoSS is an electronic registry of recording ownership of or interest in and transfers of government securities;

WHEREAS, the delivery of government securities sold by the Dealer, on a without recourse basis, to the investor's Principal Securities Account with the RoSS through the Client Interface System (CIS) Facility shall be sufficient compliance with the delivery requirement under Subsec. X238.1 of the Bangko Sentral ng Pilipinas ("BSP") Manual of Regulations for Banks and Circular No. 524, dated 31 March 2006.

WHEREAS, the Dealer is a government securities eligible dealer, accredited by the BTr to participate in the primary auction of government securities pursuant to Finance Department Order No. 141-95, as amended, and/or a bank/financial institution licensed by the SEC to deal in government securities in the secondary market;

WHEREAS, investors of government securities purchase/trade the same in the secondary market through any of the dealers;

WHEREAS, recording of ownership of or interest in government securities requires the creation/opening of a Principal Securities Account with the RoSS through the CIS Facility;

WHEREAS, to promote transparency, investor confidence and deepening of the government bond market, investors must be given adequate assistance in the opening/ creation of his/its Principal Securities Account with the RoSS ("Name-on- Registry");

NOW, *THEREFORE*, in view of the foregoing premises and the mutual covenants hereinafter provided, the parties hereby agree as follows:

Section 1. Obligations of BTr.

The BTr shall:

1. Receive instruction from the Dealer through the RoSS-CIS for the creation/ opening of the Principal Securities Account, as indicated in the Special Power of Attorney executed by the investor in favor of the Dealer for that purpose;

2. Create/open in the RoSS a Principal Securities Account for the requesting investor of scripless government securities through which all transactions affecting said securities will be recorded;

3. Provide and forward to the investor an electronic confirmation of his/its RoSS Principal Securities Account Number and notices and statements of account under any of the modes indicated in the Investor's Oath of Undertaking submitted to the BTr;

4. On relevant coupon/maturity payment dates and for payments made through the BSP, instruct the BSP to credit the regular demand deposit account (DDA) of the investor's settlement bank: *Provided*, That if the coupon/maturity payment date falls on a Saturday, Sunday, or Holiday or on a day during which business operations of the BTr is suspended, payment/s shall be made by the BTr on the next business day, without adjustment in the amount of interest to be paid.

5. Ensure that all government securities bought by investors from the Dealer are accurately recorded under the investor's Principal Securities Account or to the Securities Custody Account of the investor's designated third-party custodian.

6. Furnish the investor with Statement(s) of Securities Account, at least quarterly and whenever there is a movement in the investor's Principal Securities Account, through the investor's preferred mode of receipt of notice and/or statement;

7. Consistent with BTr Memoranda dated 28 December 2005, 12 January 2006 and 31 January 2006 and applicable BSP regulations, disallow any increase in the

holdings of beneficial owners of securities recorded in the sub-account of the Dealer, if any, existing as of 02 February 2006, for beneficial owners of securities who have either (a) declined in writing the delivery of his/its securities to a direct registry account under his or its name or a third-party custodian or (b) not responded to the Dealer's letter to the investor as regards the disposition of his/its securities. Any withdrawal or sale of the securities, either partial or total, under the sub-account of the Dealer for the beneficial owners may only be allowed if the Dealer is authorized in writing by the client/Investor. Such written authority shall be furnished by the Dealer to the BTr prior to the execution of the transaction.

Sec. 2. Obligations of the Dealer

The Dealer shall:

1. Assist the investor to open his/its individual Principal Securities Account (Name-On-Registry) with the RoSS through the CIS facility;

2. Conduct the Know your Client ("KYC") screening of its investors/clients referred to the BTr for the creation of the Principal Securities Account (Name-On-Registry) with the RoSS. In this connection it shall: (a) issue a certification to the BTr that it has conducted the necessary "KYC" screening; (b) maintain client identification records; (c) report any suspicious transaction in accordance with the provisions of R.A. No. 9160, otherwise known as the "Anti-Money Laundering Act of 2001", as amended, and its implementing rules and regulations; and whenever necessary, (d) afford BTr unchallenged access to said KYC records/documents. The same KYC or customer identification documents shall likewise be made available to regulators for verification upon request.

3. Transmit the investor's instructions to the RoSS for the creation/opening of a Principal Securities Account. For this purpose, the Dealer shall submit and/or inform the investor to submit to the BTr his/her settlement account maintained in a settlement bank of his/her choice, through which all relevant payments on the securities will be made by the BTr;

4. Upon the creation of the investor's Principal Securities Account with the BTr's RoSS to which the securities subject of a sale will be credited, immediately furnish the investor with the BTr's electronic confirmation of its creation. The Dealer shall also provide to the investor the BTr electronic confirmation that include a statement on the credited amount of securities;

5. Ensure that Special Power of Attorney (SPA) executed by client investors in their favor as agents of the former be limited, pursuant to BSP Circular No. 524;

6. Ensure that all government securities sold to investors are delivered to their appropriate Principal Securities Account with the RoSS, or to the account of the investor's designated custodian;

7. Undertake not to misuse the investor's RoSS Account No. which may come into its possession upon the creation of a Principal Securities Account for the investor or on previous transactions with the investor;

8. Acquaint/apprise investors on the rules and procedure prescribed by the BTr in connection with investment and trading of scripless government securities, including but not limited to coupon payment, redemption value/proceeds of the investor's securities, legal encumbrances, and other relevant information relative to investor's security holdings. As a minimum, investors must be apprised of the Revised RoSS Procedure on Buy and Sell of Securities and recording of transfers through the RoSS-CIS facility found in the BTr website, with particular emphasis on the feature of non-tagging of securities to GSEDs, or non-exclusivity of the selling GSEDs for subsequent transactions;

9. Whenever designated as authorized agent, provide BTr upon reasonable request, all evidence of authority to transact on the securities issued by investor to such authorized agent;

10. Whenever designated as authorized agent and/or settlement bank, ensure confidentiality and prompt delivery of all notices and statements of securities account/s to investors;

11. Ensure that all instructions transmitted to BTr concerning the securities account of clients-investors are legal, valid and duly authorized pursuant to an agreement, a special power of attorney, or any written authority executed by the client-investor in favor of the dealer; and

12. Disallow any increase in the securities holdings of clients recorded in its sub-account in the RoSS, with respect to clients who have either (a) declined in writing the delivery of his/its securities to a direct registry account under his or its name or a third-party custodian or (b) have not responded to the Dealer's letter to the investor as regards the disposition of his/its securities. The Dealer shall allow the client/investor to withdraw or sell, whether partial or total, from the said securities holdings recorded in the Dealer's sub-account only upon written request/instruction by the investor/client: *Provided*, That in case of investors who have not responded to the Dealer's letter regarding the disposition of his/its securities, the Dealer should be able to obtain from such investor a written advice that he is neither willing to take delivery nor have his securities delivered to a third-party custodian. The dealer shall furnish BTr such written request/instruction prior to the execution of the transaction.

Sec. 3. Cut Off Period. No transfer of securities shall be allowed (i) during the period of two (2) business days ending on (and including) the due date of any redemption payment of principal and (ii) during the period of two (2) business days ending on (and including) the due date of any coupon payment date (the "Closed Period"). BTr shall prevent any transfer of the securities to be recorded in the RoSS during any Closed Period. Bondholders of record as appearing in the RoSS as of the Closed Period will be treated by BTr as the beneficial owners of such securities for any relevant payment.

Sec. 4. Settlement Bank. Whenever the Dealer is designated by the investor as his/its settlement bank, it shall confirm receipt of payments from BTr intended for the investor and shall promptly and punctually credit the investor's bank account all said relevant payments on the securities. Upon the crediting of the regular demand deposit account of the Dealer with BSP for the applicable payments, the investor shall be considered as having been fully paid on his/its securities and the Dealer shall then be responsible to the investor. The BTr, its officers and employees and agents shall not be made liable for any claim, liability, or responsibility for damages or injury incurred by the investor on account of the Dealer's failure to pay/credit the investor's settlement account.

Sec. 5. Compliance with Anti-Money Laundering Law. The Dealer shall be responsible for compliance with the requirements of Anti-Money Laundering Law and other banking laws, rules and regulations relative to reporting of suspicious accounts and deposits.

Sec. 6. Limitation of Liability. The BTr, its officers, employees and agents shall not be held liable for any claim, liability or responsibility for damages or injury incurred by the investor on account of the loss of his/its securities holdings unless the loss or injury was caused by the act or omission of the BTr. Likewise, the BTr, its officers, employees and agents shall be rendered free and harmless from any liability on account of effecting instruction/s transmitted by the Dealer to the RoSS which the latter believed in good faith to have emanated from the Dealer.

Sec. 7. **Sanctions for Fraudulent Transactions**. In case the Dealer commits any fraudulent act or transaction in connection with government securities or violates any of its undertakings herein, the BTr shall have the right to impose administrative sanctions such as but not limited to dis-accreditation and/or suspension of accreditation as a government securities eligible dealer, and other administrative sanctions as may be prescribed by competent authorities without prejudice to civil or criminal prosecution in accordance with law.

Sec. 8. Amendment and Repeal. This agreement may be amended, modified or repealed by the parties in writing, by giving 30 days prior written notice.

Sec. 9. Effectivity. This agreement shall take effect immediately.

IN WITNESS WHEREOF, the parties have hereunto signed these presents this _____ at _____.

BUREAU OF THE TREASURY	[Dealer]
By:	By:
_____	_____
Treasurer of the Philippines	President & CEO

Signed in the presence of:

_____ _____

Republic of the Philippines)
_____)S.S

ACKNOWLEDGMENT

BEFORE ME, a Notary Public for and in the City of _____, personally appeared:

Name	CTC No.	Date & Place Issued
Bureau of the Treasury Rep. by the Treasurer of the Philippines	_____	_____
[Dealer] Rep. by _____	_____	_____

known to me to be the same persons who executed the foregoing instrument consisting of ____ ( ) pages, including this page where this Acknowledgment is written, and acknowledge to me that the same is their free and voluntary act and deed and of the agency/institution they represent.

WITNESS MY HAND AND NOTARIAL SEAL this _____ at _____, Philippines.

NOTARY PUBLIC

Doc. No.: _____
Page No.: _____
Book No.: _____
Series of _____

Annex B

NOTE: TO BE SUBMITTED TO THE
BUREAU OF THE TREASURY

INVESTOR'S UNDERTAKING

I/We,

For Individual Investors of legal age	*Name:* *Address:* *Civil Status:*
For Juridical Entity authorized to do business in the Philippines	*Name:* *Principal Office Address:* *Place of Incorporation:* *Name of Representative:* *Capacity/Position of Representative:*

A. Hereby agree to execute, pursuant to BSP Circular 524, a limited Special Power of Attorney in favor of either the dealing Government Securities Eligible Dealer[1] (GSED) or Securities Dealer[2] for the creation of a Principal Securities Account with the RoSS or for the execution of trade transactions (i.e. buying and selling instructions, including relaying of instructions to "the CUSTODIAN" to receive or deliver securities in order to consummate the buy/sell transactions) and to be bound by the provisions of a written Authority or a special power of attorney, or any relevant agreement I/we have entered into concerning my/our government security holdings, thereby confirming my/our authority for BTr-RoSS to carry out and execute the acts or instructions referred to in the aforesaid documents;

B. It is understood that the RoSS administered by the BTr is the official registry of ownership of or interest in government securities; that all government securities floated/originated by NG under its scripless policy are recorded in the RoSS as well as subsequent transfer of the same; and that I/we will abide by the rules and regulations of BTr-RoSS concerning government securities.

And further undertake as follows:

1. To create/open through the Client Interface System a Principal Securities Account with the RoSS to ensure that title of said scripless securities is officially recorded in my/our name and under my/our control.

2. That as a condition for the creation/opening of my/our Principal Securities Account with the RoSS, I/we have opened a bank account with (_____ *as Settlement Bank*) to which coupon and maturity proceeds and any other payments to be made on my/our

[1] Accredited by the Bureau of the Treasury
[2] Licensed by the Securities and Exchange Commission

government securities holdings will be credited; undertake to furnish the RoSS of said bank account number; and give notice at least three (3) business days prior to any coupon and/or maturity payment of any change in the Settlement Bank and/or bank account number.

3. That no transfer of securities shall be made (i) during the period of two (2) business days ending on (and including) the due date of any redemption payment of principal and (ii) during the period of two (2) business days ending on (and including) the due date of any coupon payment date (the "Closed Period"). I/We further acknowledge that the BTr shall prevent any transfer of the securities to be recorded in the RoSS during any Closed Period.

4. That in the case of outright sale transactions of government securities, including that of RTBs, I/we undertake to sell the same to any of the GSEDs or Securities Dealers, save those provided for under existing rules and regulations on government securities applicable to tax-exempt institutions, government-owned or controlled corporations and local government units. Otherwise, I/we shall have the said securities delivered to my/our agent/custodian for trading or any other transactions pursuant to a relevant written instruction/authority.

5. To receive notices and/or statements of account on a quarterly basis or whenever there is a movement in my Principal Securities Account from the RoSS through any of the following modes:
(*Please indicate choice*)

[ ] Pick-up at the RoSS
[ ] Registered Mail to Home/Office Address _____
[ ] Deliver electronically to Agent
[ ] Deliver electronically to Settlement Bank (for pick up)
[ ] Email - email address_____

In the absence of an indicated choice, I/we understand that the BTr shall electronically deliver all Notices and Statements to my/our designated settlement bank.

Note: In addition to the indicated manner of receiving notice(s) and statement(s), Investor can directly secure from the BTr written copy of any notice, statement of account, or confirmation report, subject to prior notice to and in accordance with the procedures of the BTr.

I/We hereby agree to abide with the Schedule of Fees and the manner of collection, as may be prescribed by the BTr from time to time.

6. That I/we expressly agree and acknowledge that the crediting to the regular demand deposit account of my/our settlement bank of coupons and/or redemption value due my/our scripless securities shall constitute actual receipt of payment by me/us.

7. To hold the BTr, its officers, employees and agents free and harmless against all suits, actions, damages or claims arising from failure of my/our Settlement Bank to credit my/our bank account for coupons and maturity values on due date.

8. That all instructions affecting my/our scripless securities which are transmitted to or received in good faith by the RoSS from myself/ourselves or my/our designated agent/custodian are covered by relevant documentation indicating my/our express consent and authority.

9. That I/we expressly warrant and authorize the delivery of copies of all evidence of authority granted to my/our designated agent/custodian to transact on my/our scripless securities upon reasonable demand by BTr.

10. That I/we undertake to immediately notify the RoSS of any unauthorized trade of my/our scripless securities, and until receipt of such notice, transactions effected by BTr in good faith are deemed valid.

11. To render free and harmless the BTr, its officers, employees and agents for any claim or damages with respect to trade instructions carried out in good faith.

12. That while it is understood that BTr shall maintain the strict confidentiality of records in the RoSS, I/we hereby expressly waive and authorize BTr, to the extent allowed by law, to disclose relevant information in compliance with Anti-Money Laundering laws, rules and regulations.

13. To submit to the BTr the relevant special power of attorney or authorizations issued to my/our agent, upon demand of BTr.

IN WITNESS WHEREOF, I/We hereunto affix our hands this _____ day of _____ at _____, Philippines.

_____
Name & Signature of Investor

Conforme:

_____
Settlement Bank

ACKNOWLEDGMENT

BEFORE ME, a Notary Public for and in the City of _____, personally appeared:

Name:	**CTC No.**	**Date:**	**Place of Issue:**
_____	_____	_____	_____

(Investor or Representative of Juridical Entity)

known to me to be the same person who executed the foregoing instrument and he/she acknowledged to me that the same is his/her free and voluntary act and deed (and the free act and deed of the entity they represent).

WITNESS MY HAND AND NOTARIAL SEAL this _____ at _____, Philippines.

NOTARY PUBLIC

Doc. No.: _____
Page No.: _____
Book No.: _____
Series of _____

THE GUIDELINES FOR THE IMPOSITION OF MONETARY PENALTY FOR VIOLATIONS/OFFENSES WITH SANCTIONS FALLING UNDER SECTION 37 OF R. A. NO. 7653 ON QUASI-BANKS, DIRECTORS AND/OR OFFICERS

(Appendix to Secs. 4199Q, 4299Q, 4399Q, 4499Q, 4699Q, 4799Q, 4899Q, 4999Q, 4101N.1 and Circular No. 645 dated 13 February 2009)

The schedule of penalty, categorized based on: (1) the nature of offenses such as minor, less serious, and/or serious, and (2) the assets size of the quasi-bank, shall be as follows:

A. For Serious Offense

Asset Size / Penalty Range	Up to P200 million	Above P200 million but not exceeding P500 million	Above P500 million but not exceeding P1 billion	Above P1 billion but not exceeding P10 billion	Above P10 billion but not exceeding P50 billion	Above P50 billion
Minimum	P 500	P 1, 000	P 3, 000	P 10, 000	P 18, 000	P 25, 000
Medium	750	1, 500	5, 000	12, 500	20, 000	27, 500
Maximum	1, 000	2, 000	7, 000	15, 000	22, 000	30, 000

B. For Less Serious Offense

Asset Size / Penalty Range	Up to P200 million	Above P200 million but not exceeding P500 million	Above P500 million but not exceeding P1 billion	Above P1 billion but not exceeding P10 billion	Above P10 billion but not exceeding P50 billion	Above P50 billion
Minimum	P 300	P 600	P 1, 000	P 3, 000	P 7, 000	P 15, 000
Medium	350	700	1, 250	4, 000	8, 500	17, 500
Maximum	400	800	1, 500	5, 000	10, 000	20, 000

C. For Minor Offense

Asset Size / Penalty Range	Up to P200 million	Above P200 million but not exceeding P500 million	Above P500 million but not exceeding P1 billion	Above P1 billion but not exceeding P10 billion	Above P10 billion but not exceeding P50 billion	Above P50 billion
Minimum	P 150	P 300	P 600	P 1, 000	P 3, 000	P 6, 000
Medium	200	400	700	1, 500	4, 000	8, 000
Maximum	250	500	800	2, 000	5, 000	10, 000

For purposes of this Regulation, the following definition of terms shall mean:

1. **Serious Offense** - This refers to unsafe or unsound quasi-banking practice. An unsafe or unsound practice is one (1) in which there has been some conduct, whether act or omission, which is contrary to accepted standards of prudent quasi-banking operation and may result to the exposure of the quasi-bank and its shareholders to abnormal risk or loss.

In determining the acts or omissions included under the unsafe or unsound banking practice, an analysis of the impact thereof on the banks/quasi-banks/trust entities' operations and financial condition must be undertaken, including evaluation of capital position, asset condition, management, earnings posture and liquidity position. The following circumstances shall be considered:

(a) The act or omission has resulted or may result in material loss or damage, or abnormal risk or danger to the safety, stability, liquidity or solvency of the institution;

(b) The act or omission has resulted or may result in material loss or damage or abnormal risk to the institution's depositors, creditors, investors, stockholders or to the Bangko Sentral or to the public in general;

(c) The act or omission has caused any undue injury, or has given unwarranted benefits, advantage or preference to the quasi-bank or any party in the discharge by the director or officer of his duties and responsibilities through manifest partiality, evident bad faith or gross inexcusable negligence; or

(d) The act or omission involves entering into any contract or transaction manifestly and grossly disadvantageous to the bank, quasi-bank or trust entity, whether or not the director or officer profited or will profit thereby.

Certain acts or omissions as falling under this classification maybe determined based on the guidelines provided under *Appendix Q-24*.

2. **Less Serious Offense** - These include major acts or omissions defined as quasi-bank/ individual's failure to comply with the requirements of banking laws, rules and regulations, provisions of Manual of Regulations(MOR)/Circulars/Memorandum as well as Monetary Board directives/instructions having *material*[1/] impact on quasi-bank's solvency, liquidity or profitability and/or those violations classified as major offenses under the Report of Examination, except those classified under unsafe or unsound banking practice.

3. **Minor Offense** - These include acts or omissions which are procedural in nature, can be corrected immediately and do not have material impact on the solvency, liquidity and profitability of the quasi-bank. All other acts or omissions that cannot be classified under the major offenses/violations will be classified under this category.

4. **Minimum** refers to the range of penalties to be imposed if the mitigating factor(s) outweigh the aggravating circumstances.

5. **Medium** refers to the penalty to be imposed in the absence of any mitigating and aggravating circumstances or if the mitigating factor(s) offset the aggravating factor(s).

[1/] SFAS/IAS defines materiality as any information, which if omitted or misstated, could influence the economic decisions of users taken on the basis of the financial statements. Per Financial Accounting Standard Board (FASB), it is defined as the magnitude of an omission or misstatement of accounting information.

6. **Maximum** refers to the penalty to be imposed if the aggravating circumstances outweigh the mitigating factor(s).

In determining the amount of penalty, a two-stage assessment shall be conducted as follows:

Step 1: Determine the nature of offense whether it is: (a) Serious; (b) Less Serious; or (c) Minor Offense; and

Step 2: Determine whether there are aggravating and/or mitigating factors (as listed and defined in *Annex A*).

Both the aggravating and mitigating factors shall be considered for initial penalty imposition and subsequent requests for reconsideration thereto.

The foregoing monetary penalties shall be without prejudice to the imposition of non-monetary sanctions, if and when deemed applicable by the Monetary Board. Violations of banking laws and Bangko Sentral regulations with specific penal clause are not covered by this Regulation.

(As amended by Circular Nos. 673 dated 10 December 2009 and 645 dated 13 February 2009)

Annex A

Aggravating and Mitigating Factors to be Considered in the Imposition of Penalty

1. Aggravating Factors:

(a) Frequency of the commission of specific violation – This pertains to commission or omission of a specific offense involving either the same or different transaction. This will also refer to a violation which may have been corrected in the past but found repeated in another transaction/account in the subsequent examination.

In determining frequency, the number of times of commission or omission of a specific offense during the preceding three (3) - year period shall also be considered.

The word "offense" pertains to a violation that connotes infraction of existing BSP rules and regulations as well as non-compliance with BSP/MB directives.

(b) Duration of Violations Prior to Notification – This pertains to the length of time prior to the latest notification on the violation. Violations that have been existing for a long time before it was revealed/ discovered in the regular examination or are under evaluation for a long time due to pending requests or correspondences from QBs on whether a violation has actually occurred shall be dealt with through this criterion. Violations outstanding for more than one (1) year prior to notification, at the minimum, will qualify as violations outstanding for a long time.

(c) Continuation of offense or omission after notification – This pertains to the persistence of an act or offense after the latest notification on the existence of the violation, either from the appropriate department of the SES or from the Monetary Board and/or Deputy Governor, in cases where the violation has been elevated accordingly. This covers the period after the final notification of the existence of the violation until such time that the violation has been corrected and/ or remedied. The corrective action shall be reckoned with from the date of notification.

(d) Concealment – This factor pertains to the cover up of a violation. In evaluating this factor, one shall consider the intention of the party(ies) involved and whether pecuniary benefit may accrue accordingly.

Intention precedes concealment. The act of concealing an offense or omission carries with it the intention to defraud regulators. Moreover, the amount of pecuniary benefit, which may or may not accrue from the offense or omission, shall also be considered under this factor.

Concealment may be apparent in cases when QB officers purposely complicates the transaction to make it difficult to uncover or refuse to provide information/ documents that would support the violation/offense committed.

In as much as concealment and intention are speculative matters and may be difficult to establish, appropriate support of facts or circumstantial evidence in this factor shall be considered.

(e) Loss or risk of loss to QB – In assessing this factor, "potential loss" refers to any time at which the QB was in danger of sustaining a loss.

- *Substantial actual loss* – The QB has been exposed to a significant loss of earnings and capital. The volume of accounts involved in the loss is substantial/ significant in relation to the institution's

assets and capital. The QB/individual may have substantial/serious violations that could impact the reputation and earnings of the QB.

- *Minimal actual loss or substantial risk of loss* – The QB has incurred minimal loss or will be exposed to substantial risk of loss of earnings or capital although both do not materially impact financial condition. The volume of accounts involved for minimal loss or substantial risk of loss is reasonable and manageable. While a loss was incurred, the QB could absorb the loss in the normal course of business. Substantial risk of loss includes *any potential losses the aggregate of which amounts to at least one percent (1%) of the capital of the QB*[1].
- *Minimal risk of loss* – The risk exposure on earnings or capital is minimal. QB is not vulnerable to significant loss. The volume of accounts involved for potential loss/risk is minimal/negligible. The risk of loss would have little impact on the QB or its financial condition. The risk of loss aggregating to less than one percent (1%) of the capital of the QB will fall under this classification.

(f) Impact to QB/banking industry– In assessing this factor, it is appropriate to consider any possible negative impact or harm to the QB. (e.g. A violation of law involving insider abuse may result in adverse publicity for the institution, possibly causing a run on deposits and affecting the QB's liquidity). Resulting effect on the banking industry on the violation/offenses committed by the QB, if any, will also be considered. Sources of data may come from news reports.

- *Substantial impact on QB. No impact on banking industry*. This may involve reputational risk of the QB as a result of negative publicity generated for example, by involvement of QB's director/ officer in activities not acceptable to the regulatory bodies, e.g. pyramiding, investment scams etc. This may also involve insider abuse of authority/power. However, the banking industry is not affected for this isolated case.
- *Moderate impact on banking industry or on public perception of banking industry*. This may involve poor corporate governance and mismanagement of QB that may result to erosion of public confidence leading to bank run in various branches. This may also trigger a bank run in other subsidiaries.
- *Substantial impact on banking industry or on public perception of banking industry*. This is a worst-case scenario. The violations/irregular activities of the QB may totally erode the trust and confidence of the quasi-banking public resulting to a nationwide bank run. Pessimistic perception of the banking public on the banking industry is highly observed.

2. Mitigating Factors

(a) Good Faith – Good faith is the absence of intention of the erring individual/entity in the commission of a violation.

- *Full Cooperation* - This is determined by the actions of the individual and/or QB towards the regulators after or even before notification of the offense and/ or omission. Assistance rendered by the QB during the investigation and/or examination conducted relative to the cited offense and/or omission may be viewed favorably when computing the amount of penalty to be imposed on the QB/ individual.
- *With positive measures/action undertaken although not corrected immediately*. The QB is willing to remedy/

[1] Cir. 410 dated 29 October 2003 provides that external auditors of QBs must report to BSP, among others, any potential losses the aggregate of which amounts to at least one percent (1%) of the capital to enable the BSP to take timely and appropriate remedial action.

correct the violation but is being restrained of its capacity to take immediate action thus, will undertake a Memorandum of Undertaking/Commitment for a specified period as a sign of good faith. The QB has started to rectify the infraction by instituting reforms in their operations or systems.

- Voluntary disclosure of offense - Voluntary disclosure of the QB of the offense committed before it is discovered by BSP examiners in the regular/special examination or in the supervisory work (e.g. submission of reports to the BSP disclosing the violation committed by the QB based on the internal auditor's findings) may be considered as the highest level of mitigation under this factor.

The burden of proof, however, falls on the QB/individual to support its/his/her claim of good faith and may be used as basis to mitigate the amount of penalty that may be imposed.

PROMPT CORRECTIVE ACTION FRAMEWORK

[Appendix to Secs. 4193Q (2008 - 4192Q), 4192S, 4192P and 4192N]

In carrying out its primary objective of maintaining price stability conducive to a balanced and sustainable growth of the economy[1], the BSP 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 BSP. 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 BSP, as supervisor, can enforce PCA[3] as soon as a bank's condition indicates higher-than normal risk of failure.

PCA essentially involves the BSP 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 BSP 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

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[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

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 MORNBFI);

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 FI; 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 Ratio[1], Tier 1 Risk-Based Ratio, or Leverage Ratio[2] 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. 4111Q;

(2) 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 BSP shall require the bank to enter into a MOU committing to the PCA plan. The MOU shall be subject to approval by the Monetary Board.

In order to monitor compliance with the PCA, quarterly progress reports shall be made. The BSP 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 FI may undertake;

(3) denial of application for branching and other special authorities;

(4) denial or restriction of access to BSP 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 BSP credit facilities notwithstanding non-compliance with standard conditions of access to such

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[1] Otherwise known as CAR
[2] Total Capital / Total Assets

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 Sec. 29 (conservatorship) and Sec. 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.

(Circular No. 523 dated 23 March 2006, as amended by Circular No. 664 dated 15 September 2009)

GUIDELINES FOR THE CHANGE IN THE MODE OF COMPLIANCE WITH THE LIQUIDITY RESERVE REQUIREMENT

[Appendix to Subsecs. 4254Q (2008 - 4246Q.1) & 4405Q.5]

The following guidelines shall be observed in implementing the change in the mode of compliance with the liquidity reserve requirement from holding government securities bought directly from the BSP:

1. Government securities previously bought from the BSP in compliance with the liquidity reserve requirement shall remain eligible for such purpose until these mature or are sold back to the BSP at yields quoted by the BSP Treasury Department (TD). Only the outstanding ERAP and PEACe bonds shall qualify as eligible securities for liquidity reserves. Future issuances will no longer carry the liquidity reserve eligibility under this section.

2. The interest rates applied to the RDA shall be set by the TD at one-half percent (1/2%) below the prevailing market rate for comparable government securities;

3. Pre-termination of RDAs shall be allowed subject to a reduction in applicable interest rates, as prescribed by the TD;

4. Banks and QBs shall submit on placement date a written authority (see *Annex A*) to the TD to debit their DDA with the BSP as payment for the RDA;

5. Principal and interest payments at maturity net of applicable tax shall be made by the BSP through automatic credit to the institution's DDA with the BSP. Full or partial rollover of placements in the RDA shall be settled on a gross basis;

6. Any deficiency in the liquidity reserves shall continue to be in the forms or modes prescribed under existing regulations for the composition of required reserves;

7. Banks and QBs shall continue to specify in the prescribed reports to the SDC of the BSP the balance of government securities held for liquidity reserve purposes. Said balance shall decline over time as government securities previously bought from the BSP mature or are sold back to the BSP; and

8. To facilitate the adoption of the change in the mode of compliance with the liquidity reserve requirement, the TD (while starting to accept placements in the reserve deposit account) shall continue to sell government securities for liquidity reserve purposes until 29 September 2006.

The above guidelines shall take effect on 25 August 2006.

(Circular Nos. 551 dated 17 November 2006 and 539 dated 09 August 2006)

Annex A

DEBIT/CREDIT AUTHORITY FORMAT
ORDINARY WHITE PAPER
2 COPIES

(COUNTERPARTY'S LETTERHEAD)

DATE: _____

TREASURY DEPARTMENT
TREASURY SERVICES GROUP – DOMESTIC
BANGKO SENTRAL NG PILIPINAS

GENTLEMEN:

THIS IS TO CONFIRM OUR RESERVE DEPOSIT ACCOUNT (RDA) PLACEMENT WITH YOUR OFFICE, DETAILED AS FOLLOWS:

VALUE DATE	
TERM	
MATURITY DATE	
RATE	
PRINCIPAL AMOUNT	
GROSS INTEREST	
WITHHOLDING TAX	
LIQUIDITY RESERVES FOR (PLEASE CHECK ONE)	☐ Deposit Liabilities & Deposit Substitute ☐ TOFA - Others ☐ CTF

ACCORDINGLY, PLEASE DEBIT OUR REGULAR DEMAND DEPOSIT ACCOUNT WITH YOURSELVES ON VALUE DATE FOR THE PRINCIPAL AMOUNT OF (AMOUNT IN WORDS) (₱) AND CREDIT THE SAME ACCOUNT ON MATURITY DATE THE AMOUNT OF (AMOUNT IN WORDS) (₱) REPRESENTING FULL PAYMENT OF THE PRINCIPAL PLUS INTEREST (NET OF APPLICABLE WITHHOLDING TAX) THEREON.

VERY TRULY YOURS,

(AUTHORIZED SIGNATORY)1

(AUTHORIZED SIGNATORY)2

(Circular Nos. 551 dated 17 November 2006 and 539 dated 09 August 2006)

GUIDELINES ON SUPERVISION BY RISK

[Appendix to Secs. 4173Q (2008 - 4193Q), 4193S, 4193P and 4193N]

I. Background

It must be recognized that banking is a business of taking risks in order to earn profits. While banking risks historically have been concentrated in traditional banking activities, the financial services industry has evolved in response to market-driven, technological, and legislative changes. These changes have allowed FIs to expand product offerings, geographic diversity, and delivery systems. They have also increased the complexity of the FI's consolidated risk exposure. Because of this complexity, FIs must evaluate, control, and manage risk according to its significance. The FI's evaluation of risk must take into account how non-bank activities within a banking organization affect the FI. Consolidated risk assessments should be a fundamental part of managing the FI. Large FIs assume varied and complex risks that warrant a risk-oriented supervisory approach.

II. Statement of policy

The existence of risk is not necessarily a reason for concern. Likewise, the existence of high risk in any area is not necessarily a concern, so long as management exhibits the ability to effectively manage that level of risk. Under this approach, the BSP will not necessarily attempt to restrict risk-taking but rather ensure that FIs identify, understand, and control the risks they assume. As an organization grows more diverse and complex, the FI's risk management processes must keep pace. When risk is not properly managed, BSP will direct FI management to take corrective action such as reducing exposures, increasing capital, strengthening risk management processes or a combination of these actions. In all cases, the primary concern of the BSP is that the FI operates in a safe and sound manner and maintains capital commensurate with its risks. Further guidance on risk management issues will be addressed in subsequent issuances that are part of the overall risk assessment program.

III. Guidelines for risk management

For purposes of the discussion of risk, the BSP will evaluate banking risk relative to its impact on capital and earnings. From a supervisory perspective, risk is the potential that events, expected or unanticipated, may have an adverse impact on the FI's capital or earnings.

The BSP-SES has defined eight (8) categories of risk for FI supervision purposes. These risks are: credit, market, interest rate, liquidity, operational, compliance, strategic, and reputation. These categories are not mutually exclusive; any product or service may expose the FI to multiple risks. In addition, they can be interdependent. Increased risk in one (1) category can increase risk in other categories.

Types and definitions of risk

1. *Credit risk* arises from counterparty's failure to meet the terms of any contract with the FI or otherwise perform as agreed. Credit risk is found in all activities where success depends on counterparty, issuer, or borrower performance. It arises any time FI funds are extended, committed, invested, or otherwise exposed through actual or implied contractual agreements, whether reflected on or off the balance sheet. Credit risk is not limited to the loan portfolio.

2. *Market risk* is the risk to earnings or capital arising from changes in the value

of traded portfolios of financial instruments. This risk arises from market-making, dealing, and position-taking in interest rate, foreign exchange, equity and commodities markets.

3. *Interest rate risk* is the current and prospective risk to earnings or capital arising from movements in interest rates. Interest rate risk arises from differences between the timing of rate changes and the timing of cash flows (repricing risk); from changing rate relationships among different yield curves affecting FI activities (basis risk); from changing rate relationships across the spectrum of maturities (yield curve risk); and from interest-related options embedded in FI products (options risk).

4. *Liquidity risk* is the current and prospective risk to earnings or capital arising from an FI's inability to meet its obligations when they come due without incurring unacceptable losses. Liquidity risk includes the inability to manage unplanned decreases or changes in funding sources. Liquidity risk also arises from the failure to recognize or address changes in market conditions that affect the ability to liquidate assets quickly and with minimal loss in value.

5. *Operational risk* is the current and prospective risk to earnings or capital arising from fraud, error, and the inability to deliver products or services, maintain a competitive position, and manage information. Risk is inherent in efforts to gain strategic advantage, and in the failure to keep pace with changes in the financial services marketplace. Operational risk is evident in each product and service offered. Operational risk encompasses: product development and delivery, operational processing, systems development, computing systems, complexity of products and services, and the internal control environment.

6. *Compliance risk* is the current and prospective risk to earnings or capital arising from violations of, or non-conformance with, laws, rules, regulations, prescribed practices, internal policies and procedures, or ethical standards. Compliance risk also arises in situations where the laws or rules governing certain FI products or activities of the FI's clients may be ambiguous or untested. This risk exposes the FI to fines, payment of damages, and the voiding of contracts. Compliance risk can lead to diminished reputation, reduced franchise value, limited business opportunities, reduced expansion potential, and lack of contract enforceability.

7. *Strategic risk* is the current and prospective impact on earnings or capital arising from adverse business decisions, improper implementation of decisions, or lack of responsiveness to industry changes. This risk is a function of the compatibility of an organization's strategic goals, the business strategies developed to achieve those goals, the resources deployed against these goals, and the quality of implementation. The resources needed to carry out business strategies are both tangible and intangible. They include communication channels, operating systems, delivery networks, and managerial capacities and capabilities. The organization's internal characteristics must be evaluated against the impact of economic, technological, competitive, regulatory, and other environmental changes.

8. *Reputation risk* is the current and prospective impact on earnings or capital arising from negative public opinion. This affects the FI's ability to establish new relationships or services or continue servicing existing relationships. This risk may expose the FI to litigation, financial loss, or a decline in its customer base. In extreme cases, FIs that lose their reputation may suffer a run on deposits. Reputation risk exposure is present throughout the organization and requires the responsibility to exercise an abundance of caution in dealing with customers and the community.

IV. FI management of risk

Because market conditions and company structures vary, there is no single risk management system that works for all FIs. Each FI should tailor its risk management program to its needs and circumstances. Sound risk management systems, however, have several things in common; for example, they are independent of risk-taking activities. Regardless of the risk management program's design, each program should:

1. *Identify risk*: To properly identify risks, an FI must recognize and understand existing risks or risks that may arise from new business initiatives, including risks that originate in non-bank subsidiaries and affiliates. Risk identification should be a continuing process, and should occur at both the transaction and portfolio level.

2. *Measure risk*: Accurate and timely measurement of risk is essential to effective risk management systems. An FI that does not have a risk measurement system has limited ability to control or monitor risk levels. Further, the more complex the risk, the more sophisticated should be the tools that measure it. An FI should periodically conduct tests to make sure that the measurement tools it uses are accurate. Good risk measurement systems assess the risks of both individual transactions and portfolios. During the transition process in FI mergers and consolidations, the effectiveness of risk measurement tools is often impaired because of the technological incompatibility of the merging systems or other problems of integration. Therefore, the resulting FI must make a strong effort to ensure that risks are appropriately measured across the consolidated entity. Larger, more complex FIs must assess the impact of increased transaction volume across all risk categories.

3. *Monitor risk*: FIs should monitor risk levels to ensure timely review of risk positions and exceptions. Monitoring reports should be frequent, timely, accurate, and informative and should be distributed to appropriate individuals to ensure action, when needed. For large, complex FIs, monitoring is essential to ensure that management's decisions are implemented for all geographies, products, and legal entities.

4. *Control risk*: The FI should establish and communicate risk limits through policies, standards, and procedures that define responsibility and authority. These control limits should be valid tools that management should be able to adjust when conditions or risk tolerances change. The FI should have a process to authorize exceptions or changes to risk limits when warranted. In merging or consolidating FIs, the transition should be tightly controlled; business plans, lines of authority, and accountability should be clear. Large, diversified FIs should have strong risk controls covering all geographies, products, and legal entities.

The Board must establish the FI's strategic direction and risk tolerances. In carrying out these responsibilities, the Board should approve policies that set operational standards and risk limits. Well-designed monitoring systems will allow the Board to hold management accountable for operating within established tolerances. Capable management and appropriate staffing are also essential to effective risk management. FI management is responsible for the implementation, integrity, and maintenance of risk management systems. Management also must keep the directors adequately informed. Management must:

a. Implement the FI's strategy;

b. Develop policies that define the FI's risk tolerance and ensure that they are compatible with strategic goals;

c. Ensure that strategic direction and risk tolerances are effectively communicated and adhered to throughout the organization;

d. Oversee the development and maintenance of management information systems to ensure that information is timely, accurate, and pertinent.

V. Assessment of risk management

When assessing risk management systems, the BSP will consider the FI's policies, processes, personnel, and control systems. Significant deficiencies in any one of these areas will cause the BSP to expect the FI to compensate for these deficiencies in their overall risk management process.

1. *Policies* are statements of the FIs' commitment to pursue certain results. Policies often set standards (on risk tolerances, for example) and recommend courses of action. Policies should express an FI's underlying mission, values, and principles. A policy review should always be triggered when an FI's activities or risk tolerances change.

2. *Processes* are the procedures, programs, and practices that impose order on the FI's pursuit of its objectives. Processes define how daily activities are carried out. Effective processes are consistent with the underlying policies, are efficient, and are governed by checks and balances.

3. *Personnel* are the staff and managers that execute or oversee processes. Good staff and managers perform as expected, are qualified, and competent. They understand the FI's mission, values, policies, and processes. Compensation programs should be designed to attract, develop, and retain qualified personnel. In addition, compensation should be structured to reward contributions to effective risk management.

4. *Control systems* include the tools and information systems (e.g, internal/ external audit programs) that FI managers use to measure performance, make decisions about risk, and assess the effectiveness of processes. Feedback should be timely, accurate, and pertinent.

VI. Supervision by Risk

Using the core assessment standards of the BSP as guide, an examiner will obtain both a current and prospective view of an FI's risk profile. When appropriate, this profile will incorporate potential material risks to the FI from non-bank affiliates' activities conducted by the FI. Subsidiaries and branches of foreign FIs should maintain sufficient documentation onsite to support the analysis of their risk management. This risk assessment drives supervisory strategies and activities. It also facilitates discussions with FI management and directors and helps to ensure more efficient examinations. The core assessment complements the risk assessment system (RAS). Examiners document their conclusions regarding the quantity of risk, the quality of risk management, the level of supervisory concern (measured as aggregate risk), and the direction of risk using the RAS. Together, the core assessment and RAS give the appropriate department of the SES the means to assess existing and emerging risks in FIs, regardless of size or complexity.

Specifically, supervision by risk allocates greater resources to areas with higher risks. The appropriate department of the SES will accomplish this by:

1. Identifying risks using common definitions. The categories of risk, as they are defined, are the foundation for supervisory activities.

2. Measuring risks using common methods of evaluation. Risk cannot always

be quantified in pesos. For example, numerous internal control deficiencies may indicate excessive operational risk.

3. Evaluating risk management to determine whether FI systems and processes permit management to manage and control existing and prospective levels of risk.

The appropriate department of the SES will discuss preliminary conclusions regarding risks with FI management. Following these discussions, it will adjust conclusions when appropriate. Once the risks have been clearly identified and communicated, it can then focus supervisory efforts on the areas of greater risk within the FI, the consolidated banking organization, and the banking system.

To fully implement supervision by risk, the appropriate department of the SES will also assign CAMELS ratings to the lead FI and all affiliated FIs. It may determine that risks in individual FIs are increased, reduced, or mitigated in light of the consolidated risk profile of the FI as a whole. To perform a consolidated analysis, it obtain pertinent information from FIs and affiliates, and verify transactions flowing between FIs and affiliates.

(Circular No. 510 dated 03 February 2006)

GUIDELINES ON MARKET RISK MANAGEMENT

[Appendix to Sec. 4174Q (2008 - 4194Q), 4194S, 4194P and 4194N]

I. Background

The globalization of financial markets, increased transaction volume and volatility, and the introduction of complex products and trading strategies have made market risk management take on a more important role in risk management. FIs now use a wide range of financial products and strategies, ranging from the most liquid fixed income securities to complex derivative instruments and structured products. The risk dimensions of these products and strategies must be fully understood, monitored, and controlled by a FI.

II. Statement of policy

For purposes of these guidelines, FIs refer to banks and NBFIs supervised by the BSP and their respective financial subsidiaries. The level of market risk assumed by an FI is not necessarily a concern, so long as the FI has the ability to effectively manage the risk. Therefore, the BSP will not restrict the level of risk assumed by an FI, or the scope of its financial market activities, so long as the FI is authorized to engage in such activities and:

- Understands, measures, monitors and controls the risk assumed,
- Adopts risk management practices whose sophistication and effectiveness are commensurate to the risk being monitored and controlled, and
- Maintains capital commensurate with the risk exposure assumed.

If the BSP determines that an FI's risk exposures are excessive relative to the FI's capital, or that the risk assumed is not well managed, the BSP will direct the FI to reduce its exposure to an appropriate level and/or strengthen its risk management systems.In evaluating the above parameters, the BSP expects FIs to have sufficient knowledge, skills and appropriate system and technology necessary to understand and effectively manage their market risk exposures. The principles set forth in these guidelines shall be used in determining the adequacy and effectiveness of an FI's market risk management process, the level and trend of market risk exposure and adequacy of capital relative to exposure. The BSP shall consider the following factors:

1. The major sources of market risk exposure and the complexity and level of risk posed by the assets, liabilities, and off-balance-sheet activities of the FI;
2. The FI's actual and prospective level of market risk in relation to its earnings, capital, and risk management systems;
3. The adequacy and effectiveness of the FI's risk management practices and strategies as evidenced by:

- The adequacy and effectiveness of board and senior management oversight;
- Management's knowledge and ability to identify and manage sources of market risk as measured by past and projected financial performance;
- The adequacy of internal measurement, monitoring, and management information systems;
- The adequacy and effectiveness of risk limits and controls that set tolerances on income and capital losses;
- The adequacy and frequency of the FI's internal review and audit of its market risk management process.

Further, an FI's market risk management system shall be assessed under the FI's general risk management framework, consistent with the guidelines on supervision by risk as set forth under *Appendix Q-42*.

III. Market risk management process

An FI's market risk management process should be consistent with its general risk management framework and should be commensurate with the level of risk assumed. Although there is no single market risk management system that works for all FIs, an FI's market risk management process should:

1. *Identify market risk*. Identifying current and prospective market risk exposures involves understanding the sources of market risk arising from an FI's existing or new business initiatives. An FI should have procedures in place to identify and address the risk posed by new products and activities prior to initiating the new products or activities.

Identifying market risk also includes identifying an FI's desired level of risk exposure based on its ability and willingness to assume market risk. An FI's ability to assume market risk depends on its capital base and the skills/capabilities of its management team. In any case, market risk identification should be a continuing process and should occur at both the transaction and portfolio level.

2. *Measure market risk*. Once the sources and desired level of market risk have been identified, market risk measurement models can be applied to quantify an FI's market risk exposures. However, market risk cannot be managed in isolation. Market risk measurement systems should be integrated into an FI's general risk measurement system and results from models should be interpreted in coordination with other risk exposures. Further, the more complex an FI's financial market activities are, the more sophisticated the tools that measure market risk exposures arising from such complex activities should be.

3. *Control market risk*. Quantifying market risk exposures help an FI align existing exposures with the identified desired level of exposures. Controlling market risk usually involves establishing market risk limits that are consistent with an FI's market risk measurement methodologies. Limits may be applied through an outright prohibition on exposures above a pre-set threshold, by restraining activities or deploying strategies that alter the risk-return characteristics of on- and off- balance sheet positions. Appropriate pricing strategies may likewise be used to control market risk exposures.

4. *Monitor market risk***.** Ensuring that market risk exposures are adequately controlled requires the timely review of market risk positions and exceptions. Monitoring reports should be frequent, timely and accurate. For large, complex FIs, consolidated monitoring should be employed to ensure that management's decisions are implemented for all geographies, products, and legal entities.

IV. Definition and sources of market risk

Market risk is the risk to earnings or capital arising from adverse movements in factors that affect the market value of instruments, products, and transactions in an institution's overall portfolio, both on or off-balance sheet. Market risk arises from market-making, dealing, and position-taking in interest rate, foreign exchange, equity and commodities markets.

Interest rate risk is the current and prospective risk to earnings or capital arising from movements in interest rates.

FX risk refers to the risk to earnings or capital arising from adverse movements in FX rates.

Equity risk is the risk to earnings or capital arising from movements in the value of an institution's equity-related holdings.

Commodity risk is the risk to earnings or capital due to adverse changes in the value of an institution's commodity-related holdings.

While there are generally four sources of market risk, as defined herein, the focus

of this Appendix is *interest rate risk* and *FX risk*. Nevertheless, the principles set forth in the market risk management process and sound risk management practices are generally applicable to all sources of market risk.

a. Interest rate risk

Interest rate risk is the risk that changes in market interest rates will reduce current or future earnings and/or the economic value of a FI. Accepting interest rate risk is a normal part of financial intermediation and is a major source of profitability and shareholder value. Excessive or inadequately understood and controlled interest rate risk, however, can pose a significant threat to an FI's earnings and capital. Thus, an effective risk management process that maintains interest rate risk within prudent levels is essential to the safety and soundness of FIs.

1. Sources of interest rate risk

a. *Re-pricing risk*

This is the most common type of interest rate risk and arises from differences in the maturity (for fixed-rate instruments) and re-pricing (for floating-rate instruments) of an FI's assets, liabilities and off-balance sheet positions. While such re-pricing mismatches are fundamental to the business of financial intermediation, they also expose an FI's earnings and underlying economic value to changes based on fluctuations in market interest rates.

b. *Basis risk*

Basis risk arises from imperfect correlations among the various interest rates earned and paid on financial instruments with otherwise similar re-pricing characteristics. A shift in the relationship between these rates or interest rates in different markets can give rise to unexpected changes in the cash flows and earnings spread between assets, liabilities and off-balance sheet instruments of similar maturities or re-pricing frequencies.

c. *Yield curve risk*

Yield curve risk is the risk that rates of different maturities may change by a different magnitude. It arises from variations in the movement of interest rates across the maturity spectrum of the same index or market. Yield curves can steepen, flatten or even invert. Unanticipated shifts of the yield curve may have adverse effects on an FI's earnings or underlying economic value.

d. *Option risk*

Option risk is the risk that the payment patterns of assets and liabilities will change when interest rates change. Formally, an option gives the option holder the right, but not the obligation to buy, sell, or in some manner alter the cash flow of an instrument or financial contract. Options may be stand-alone instruments or may be embedded within otherwise standard instruments. Examples of instruments with embedded options include various types of bonds, notes, loans or even deposits which give a counter-party the right to prepay or even extend the maturity of an instrument or to change the rate paid. In some cases, the holder of an option can force a counter-party to pay additional notional, or to forfeit notional already paid.

The option holder's ability to choose to alter cash flows creates an asymmetric performance pattern. If not adequately managed, the asymmetrical pay-off characteristics of instruments with optionality can pose significant risk particularly to those who sell the options, since the options held, both explicit and embedded, are generally exercised to the advantage of the holder and the disadvantage of the seller.

2. Measuring the effects of interest rate risk

Changes in interest rates affect both earnings and the economic value of an FI. This has given rise to two separate, but complementary, perspectives for evaluating an FI's exposure to interest rate risk.

Exposure to earnings typically receives the most attention. Many FIs use a modified interest rate gap or earnings simulation model to forecast earnings over a running next twelve (12) month time horizon under a variety of interest rate scenarios. Given that a large portion of a typical FI's liabilities and even assets re-price in less than one (1) year, there is value in such a system. For example, earnings are a key measure in determining if the board of directors is creating value for the shareholders.

However, earnings over the next twelve (12) months do not present a complete picture of an FI's exposure to interest rate risk. Many FIs hold assets such as bonds and fixed rate loans with extended terms. The full effect of changes in interest rates on the value of these assets cannot be fully captured by a short-term earnings model. Thus, it is also important to consider a more comprehensive picture of the FI's exposure to interest rate risk through an assessment of the FI's economic value.

The BSP will not consider market risk to be "well managed" unless the FI has fully implemented an effective risk measurement system whose sophistication is commensurate with the nature and complexity of the risk assumed. Smaller FIs with non-complex single currency balance sheets may be able to use a single non-complex measurement methodology, such as re-pricing gap analysis to manage their interest rate risk. However, large commercial or universal banks with complex, multi-currency balance sheets, or FIs that accept large exposures of interest rate risk relative to capital will be expected to measure interest rate risk through a combination of earnings simulation and economic value. Trading activities should continue to be managed through the use of an effective, and independently validated Value-at-Risk (VaR) methodology.

a. *Earnings perspective*

An FI should consider how changes in interest rates may affect future earnings. The focus of analysis under the earnings perspective is the impact of changes in interest rates on accrual or reported earnings. Volatility in earnings should be monitored and controlled because reduced earnings or outright losses can threaten the financial stability of an FI by undermining its capital adequacy. Further, unexpected volatility in earnings can undermine an FI's reputation and result in an erosion of public confidence.

Fluctuations in interest rates generally have the greatest impact on reported earnings through changes in net interest income (i.e., the difference between total interest income and total interest expense). Thus, the BSP will expect FIs to adopt systems that are capable of estimating changes to net interest income under a variety of interest rate scenarios. For example, non-complex FIs with traditional business lines and balance sheets could potentially limit their simulations to a single ±100 basis point parallel rate shock. However, FIs that hold significant levels of derivatives and structured products relative to capital should incorporate more severe rate movements (e.g., ± 100, 200 and 300 basis points) to determine what happens if strike prices are breached or "events" are triggered. Further, the BSP will expect an FI to employ alternative scenarios such as changes to the shape of the yield curve if the FI is exposed to significant levels of yield curve or basis risk.

Changes in market interest rates may also affect the volume of activities that generate fee income and other non-interest income. Thus, FIs should incorporate a broader focus on overall net income – incorporating both interest and non-interest income and expenses – if the FI reports significant levels of interest rate sensitive non-interest income.

b. *Economic value perspective*

The economic value of an FI can be viewed as the present value of an FI's

expected net cash flows, defined as the expected cash flows from assets minus the expected cash flows from liabilities plus the expected net cash flows on off-balance sheet positions. As such, it provides a more comprehensive view of the potential long-term effects of changes in interest rates than is offered by the earnings perspective.

While a variety of models are available, the BSP expects that economic value models will incorporate all significant classes of assets, liabilities and off-balance sheet. As with earnings at risk, the FI should incorporate a variety of interest rate scenarios to ensure that any strike prices, caps, limits, or "events" are breached in the simulation. Also, FIs with significant levels of basis or yield curve risk are expected to add scenarios such as alternative correlations between interest rates and/or a flatter or steeper yield curve.

Managing earnings and economic exposures

Management must make certain trade-offs when immunizing earnings and economic value from interest rate risk. When earnings are immunized, economic value becomes more vulnerable, and vice versa. The economic value of equity, like that of other financial instruments, is a function of the discounted net cash flows it is expected to earn in the future. If an FI has immunized earnings, such that expected earnings remain constant for any change in interest rates, the discounted value of those earnings will be lower if interest rates rise. Hence, its economic value will fluctuate with rate changes. Conversely, if an FI fully immunizes its economic value, its periodic earnings must increase when rates rise and decline when interest rates fall.

b. FX risk

FX risk is the risk to earnings or capital arising from changes in FX rates.

In contracting to meet clients' foreign currency needs or simply buying and selling FX for its own account, a FI undertakes a risk that exchange rates might change subsequent to the time the contract is consummated. FX risk may also arise from maintaining an open FX position. Thus, managing FX risk includes monitoring an FI's net FX position.

An FI has a net position in a foreign currency when its assets, including spot and future contracts to purchase, and its liabilities, including spot and future contracts to sell, in that currency are not equal. An excess of assets over liabilities is called a net "long" position and liabilities in excess of assets, a net "short" position.

It should be noted that when engaging in FX activities, FIs are also exposed to other risks including liquidity and credit risks, particularly related to the settlement of FX contracts. FIs should have an integrated approach to risk management in relation to its FX activities: FX risk should be reviewed together with other risks to determine the FI's overall risk profile. Liquidity and settlement risks related to FX activities are outside the scope of these guidelines. Nevertheless, future guidelines may be issued on these risk areas.

V. Sound market risk management practices

When assessing an FI's market risk management system, the BSP expects an FI to address the four (4) basic elements of a sound risk management system:

1. Active and appropriate Board and senior management oversight;
2. Adequate risk management policies and procedures;
3. Appropriate risk measurement methodologies, limits structure, monitoring and management information systems; and

4. Comprehensive internal controls and independent audits.

The specific manner in which an FI applies these elements in managing its market risk will depend upon the complexity and nature of its activities, as well as the level of market risk exposure assumed. What constitutes adequate market risk management practices can therefore vary considerably. Regardless of the systems used, the BSP will not consider market risk to be well managed unless all four of the above elements are deemed to be at least "satisfactory".

As with other risk factor categories, banking groups (banks and subsidiaries/ affiliates) should monitor and manage market risk exposures of the group on a consolidated and comprehensive basis. At the same time, however, FIs should fully recognize any legal distinctions and possible obstacles to cash flow movements among affiliates and adjust their risk management practices accordingly. While consolidation may provide a comprehensive measure in respect of market risk, it may also underestimate risk when positions in one affiliate are used to offset positions in another affiliate. This is because a conventional accounting consolidation may allow theoretical offsets between such positions from which an FI may not in practice be able to benefit because of legal or operational constraints.

A. Active and appropriate board and senior management oversight[1]

Effective board and senior management oversight of an FI's market risk activities is critical to a sound market risk management process. It is important that these individuals are aware of their responsibilities with regard to market risk management and how market risk fits within the organization's overall risk management framework.

Responsibilities of the board of directors

The board of directors has the ultimate responsibility for understanding the nature and the level of market risk taken by the FI. In order to carry out its responsibilities, the Board should:

1. Establish and guide the FI's strategic direction and tolerance for market risk. While it is not possible to provide a comprehensive list of documents to consider, the BSP should see a clear and documented pattern whereby the Board reviews, discusses and approves strategies and policies with respect to market risk management. In addition, there should be evidence that the Board periodically reviews and discusses the overall objectives of the FI with respect to the level of market risk acceptable to the FI.

2. Identify senior management who has the authority and responsibility for managing market risk and ensure that senior management takes the necessary steps to monitor and control market risk consistent with the approved strategies and policies. The BSP should be able to discern a clear hierarchal structure with a clear assignment of responsibility and authority.

3. Monitor the FI's performance and overall market risk profile, ensuring that the level of market risk is maintained within tolerance and at prudent levels supported by adequate capital. The Board should be regularly informed of the market risk exposure of the FI and any breaches to established limits for appropriate action. Reporting should be timely and clearly

[1] This section refers to a management structure composed of a board of directors and senior management. The BSP is aware that there may be differences in some FIs as regards the organizational framework and functions of the board of directors and senior management. For instance, branches of foreign banks have board of directors located outside of the Philippines and are overseeing multiple branches in various countries. In this case, "board-equivalent" committees are appointed. Owing to these differences, the notions of the board of directors and the senior management are used in these guidelines not to identify legal constructs but rather to label two decision-making functions within a FI.

presented. In assessing an FI's capital adequacy for market risk, the Board should consider the FI's current and potential market risk exposure as well as other risks that may impair the FI's capital, such as credit, liquidity, operational, strategic, and reputation risks.

4. Ensure that the FI implements sound fundamental principles that facilitate the identification, measurement, monitoring and control of market risk. The board of directors should encourage discussions among its members and senior management – as well as between senior management and others in the FI – regarding the FI's market risk exposures and management process.

5. Ensure that adequate resources, both technical and human resources, are devoted to market risk management. While board members need not have detailed technical knowledge of complex financial instruments, legal issues or sophisticated risk management techniques, they have the responsibility to ensure that the FI has personnel available who have the necessary technical skills to evaluate and control market risk. This responsibility includes ensuring that there is continuous training of personnel on market risk management and providing competent technical staff for the internal audit function.

Responsibilities of senior management

Senior management is responsible for ensuring that market risk is adequately managed for both long-term and day-to-day basis. In managing the FI's activities, senior management should:

1. Develop and implement policies, procedures and practices that translate the board's goals, objectives and risk tolerances into operating standards that are well understood by personnel and that are consistent with the board's intent. Senior management should also periodically review the organization's market risk management policies and procedures to ensure that they remain appropriate and sound.

2. Ensure adherence to the lines of authority and responsibility that the board has established for measuring, managing, and reporting market risk exposures.

3. Maintain appropriate limits structure, adequate systems for measuring market risk, and standards for measuring performance.

4. Oversee the implementation and maintenance of management information and other systems to identify, measure, monitor, and control the FI's market risk.

5. Establish effective internal controls over the market risk management process.

6. Ensure that adequate resources are available for evaluating and controlling market risk. Senior management of FIs, including branches of foreign banks, should ensure that analysis and market risk management activities are conducted by competent staff with technical knowledge and experience consistent with the nature and scope of the FI's activities. There should be sufficient depth in staff resources to manage these activities and to accommodate the temporary absence of key personnel and normal succession.

In evaluating the quality of oversight, the BSP shall evaluate how the board and senior management carry out the above functions/responsibilities. Further, sound management oversight is highly related to the quality of other areas/elements of an FI's risk management system. Thus, even if board and senior management exhibit active oversight, the FI's policies, procedures, measurement methodologies, limits structure, monitoring and information systems, controls and audit must be considered adequate before quality of board and senior management can be considered at least "satisfactory".

Lines of responsibility and authority

FIs should clearly define the individuals and/or committees responsible for managing market risk and should ensure that there is adequate separation of duties in key elements of the risk management process to avoid potential conflicts of interest. Management should ensure that sufficient safeguards exist to minimize the potential that individuals initiating risk-taking positions may inappropriately influence key control functions of the market risk management process. FIs should therefore have risk measurement, monitoring, and control functions with clearly defined duties that are sufficiently independent from position-taking functions of the FI and which report risk exposures directly to the board of directors.

The nature and scope of safeguards to minimize potential conflicts of interest should be in accordance with the size and structure of an FI. Larger or more complex FIs should have a designated independent unit responsible for the design and administration of the FI's market risk measurement, monitoring and control functions.

B. Adequate risk management policies and procedures

An FI's market risk policies and procedures should be clearly defined, documented and duly approved by the board of directors. Policies and procedures should be consistent with the nature and complexity of the FI's activities. When reviewing banking groups, the BSP will assess whether adequate and effective policies and procedures have been adopted and implemented across all levels of the organization.

Policies and procedures should delineate lines of responsibility and accountability and should clearly define authorized instruments, hedging strategies, position-taking opportunities, and the market risk models used to quantify market risk. Market risk policies should also identify quantitative parameters that define the acceptable level of market risk for the FI. Where appropriate, limits should be further specified for certain types of instruments, portfolios, and activities. All market risk policies should be reviewed periodically and revised as needed. Management should define the specific procedures to be used for identifying, reporting and approving exceptions to policies, limits, and authorizations.

It is important that FIs identify market risk, as well as other risks, inherent in new products and activities and ensure these are subject to adequate procedures and controls before the new products and activities are introduced or undertaken. Specifically, new products and activities should undergo a careful pre-acquisition review to ensure that the FI understands their market risk characteristics and can incorporate them into its risk management process. Major hedging or risk management initiatives should be approved in advance by the board or its appropriate delegated committee.

Proposals and the subsequent new product/activity review should be formal and written. For purposes of managing market risk inherent in new products, proposals should, at a minimum, contain the following features:

1. Description of the relevant product or strategy;
2. Use/purpose of the new product/ activity;
3. Identification of the resources required and unit/s responsible for establishing sound and effective market risk management of the product or activity;
4. Analysis of the reasonableness of the proposed activities in relation to the FI's overall financial condition and capital levels; and

5. Procedures to be used to measure, monitor, and control the risks of the proposed product or activity.

C. Appropriate risk measurement methodologies, limits structure, monitoring, and management information system

Market risk measurement models/ methodologies

It is essential that FIs have market risk measurement systems that capture all material sources of market risk and that assess the effect of changes in market risk factors in ways that are consistent with the scope of their activities. Depending upon the size, complexity, and nature of activities that give rise to market risk, the ability to capture all material sources of market risk in a timely manner may require an FI's market risk measurement system to be interfaced with other systems, such as the treasury system or loan system. The assumptions underlying the measurement system should be clearly understood by risk managers and senior management.

Market risk measurement systems should:

1. Assess all material market risk associated with an FI's assets, liabilities, and off-balance sheet positions;

2. Utilize generally accepted financial concepts and risk measurement techniques; and

3. Have well-documented assumptions and parameters.

There are a number of methods/ techniques for measuring market risks. Complexity ranges from simple marking-to-market or valuation techniques to more advanced static simulations using current holdings to highly sophisticated dynamic modeling techniques that reflect potential future business activities. In designing market risk measurement systems, FIs should ensure that the degree of detail regarding the nature of their positions is commensurate with the complexity and risk inherent in those positions.

At a minimum, smaller non-complex FIs should have the ability to mark-to-market or revalue their investment portfolio and construct a simple re-pricing gap. When using gap analysis, the precision of interest rate risk measurement depends in part on the number of time bands into which positions are aggregated. Clearly, aggregation of positions/cash flows into broad time bands implies some loss of precision. In addition, the use of reasonable and valid assumptions is important for a measurement system to be precise. In practice, the FI must assess the significance of the potential loss of precision in determining the extent of aggregation and simplification to be built into the measurement approach. Assumptions and limitations of the measurement approach, such as the loss of precision, should be documented.

On the other hand, banks holding an expanded derivatives license and FIs engaging in options or structured products with embedded options cannot capture all material sources of market risk by using static models such as the re-pricing gap. These FIs should have interest rate risk measurement systems that assess the effects of rate changes on both earnings and economic value. These systems should provide meaningful measures of an FI's current levels of interest rate risk exposure, and should be capable of identifying any excessive exposures that might arise. Pricing models and simulation techniques will probably be required.

There is also a question on the extent to which market risk should be viewed on a whole institution basis or whether the trading book, which is marked to market, and the accrual book, which is often not, should be treated separately. As a general rule, it is desirable for any measurement

system to incorporate market risk exposures arising from the full scope of an FI's activities, including both trading and non-trading sources. A single measurement system can facilitate analysis of market risk exposure. However, this does not preclude different measurement systems and risk management approaches being used for similar or different activities. For example, a bank with expanded derivatives license will use pricing models as basic tools in valuing position from its derivatives activities and structured products. In addition, the bank should use simulation models to assess the potential effects of changes in market risk factors by simulating the future path of market risk factors and their impact on cash flows from these activities.

Different methodologies may also be applied to the trading and accrual books. Regardless of the number of models or measurement systems used, management should have an integrated view of market risk across products and business lines.

Regardless of the measurement system used, the BSP will expect the FI to ensure that input data are timely and correct, assumptions can be supported and are valid, the methodologies used produce accurate results, and the results can be easily understood by senior management and the board.

(1) Model input. All market risk measurement methodologies require various types of inputs, including hard data, readily observable parameters such as asset prices, and both quantitatively and qualitatively-derived assumptions. This applies equally to simple gap as well as complex simulation models.

The integrity and timeliness of data is a key component of the market risk measurement process. The BSP expects that adequate controls will be established to ensure that all material positions and cash flows from on- and off- balance sheet positions are incorporated into the measurement system on a consistent and timely basis. Inputs should be verified through a process that validates data integrity. Assumptions and inputs should be subject to control and oversight review. Any manual adjustments to underlying data should be documented, and the nature and reasons for the adjustments should also be clearly understood.

Critical to model accuracy is the validity of underlying assumptions. Assumptions regarding maturity of deposits, for example, are critical in measuring interest rate risk. The treatment of positions where behavioral maturity is different from contractual maturity requires the use of assumptions and may complicate the measurement of interest rate risk exposure, particularly when using the economic value approach. The validity of correlation assumptions to aggregate market risk exposures is likewise important as breakdowns in correlations may significantly affect the validity of model results. Key assumptions should therefore be subject to rigorous documentation and review. Any significant changes should be approved in advance by the board of directors.

(2) Model risk. While accuracy is key to an effective market risk measurement system, methodologies cannot be expected to flawlessly predict potential losses arising from market risk. The use of models introduces the potential for model risk. Thus, model risk is the risk of loss arising from inaccurate or incorrect quantification of market risk exposures due to weaknesses in market risk methodologies. It may arise from relying on assumptions that are inconsistent with market realities, from employing input parameters that are unreliable, or from calibrating, applying and implementing models incorrectly.

Model risk is more likely to arise for instruments that have non-standard or option-like features. The use of proprietary models that employ unconventional techniques that are not widely agreed upon by market participants is likewise more sensitive to model risk. Even the use of standard models may lead to errors if the financial tools are not appropriate for a given instrument.

The BSP expects FIs to implement effective policies and procedures to manage model risk. The scope of policies and procedures will depend upon the type and complexity of models developed or purchased. However, FIs holding an expanded license or significant levels of complex investments including structured products, should at a minimum implement the following controls:

a. Model development/acquisition, implementation and revisions. The BSP expects larger, complex FIs to adopt policies governing development/ acquisition, implementation and revision of market risk models. These policies should clearly define the responsibilities of staff involved in the development/ acquisition process. FIs should ensure that modeling techniques and assumptions are consistent with widely accepted financial theories and market practices. Policies and procedures should be duly approved by the board of directors and properly documented. An inventory of the models in use should be maintained along with documentation explaining how they operate.

The BSP also expects that revisions to models will be performed in a controlled environment by authorized personnel and changes should be made or verified by a control function. Written policies should specify when changes to models are acceptable and how those revisions should be accomplished.

b. Model validation. Before models are authorized for use, they should be validated by individuals who are neither directly involved in the development process nor responsible for providing inputs to the model. Independent model validation is a key control in the model development process and should be specifically addressed in an FI's policies. Further, the BSP expects that the staff validating the models will have the necessary technical expertise.

A sound validation process should rigorously and comprehensively evaluate the sensitivity of the model to material sources of model risk and includes the following:

1. Tests of internal logic and mathematical accuracy;

2. Development of empirical support for the model's assumptions;

3. Back-testing. The BSP expects FIs to conduct backtesting of model results. Back-testing is a method of periodically evaluating the accuracy and predictive capability of an FI's market risk measurement system by monitoring and comparing actual movements in market prices or market risk factors with projections produced by the model. To be more effective, back-testing should be conducted by parties independent of those developing or using the model. Policies should address the scope of the back-testing process, frequency of back-testing, documentation requirements, and management responses. Complex models should be back-tested continually while simple models can be back-tested periodically. Significant discrepancies should prompt a model review.

4. Periodic review of methodologies and assumptions. The BSP expects that FIs will periodically review or reassess their modeling methodologies and assumptions. Again, the frequency of review will depend on the model but

complex models should be reviewed at least once a year, when changes are made, or when a new product or activity is introduced. Model review could also be prompted when there is a need for the model to be updated to reflect changes in the FI or market. The review process should be performed by an independent group as it is considered to be part of the risk control and audit function.

The use of vendor models can present special challenges, as vendors often claim proprietary privilege to avoid disclosing information about their models. Thus, FIs may be constrained from performing validation procedures related to internal logic, mathematical accuracy and model assumptions. However, vendors should provide adequate information on how the models were constructed and validated so that FIs have reasonable assurances that the model works as intended.

c. Stress testing

The underlying statistical models used to measure market risk summarize the exposures that reflect the most probable market conditions. Regardless of size and complexity of activities, the BSP expects FIs to supplement their market risk measurement models with stress tests. Stress testing are simulations that show how a portfolio or balance sheet might perform during extreme events or highly volatile markets.

Stress testing should be designed to provide information on the kinds of conditions under which the FI's strategies or positions would be most vulnerable. Thus stress tests must be tailored to the risk characteristics of the FI. Possible stress scenarios might include abrupt changes in the general level of interest rates, changes in the relationships among key market rates (i.e., basis risk), changes in the slope and the shape of the yield curve (i.e., yield curve risk), changes in the liquidity of key financial markets, or changes in the volatility of market rates.

In addition, stress scenarios should include conditions under which key business assumptions and parameters break down. The stress testing of assumptions used for illiquid instruments and instruments with uncertain contractual maturities are particularly critical to achieving an understanding of the FI's risk profile. When conducting stress tests, special consideration should be given to instruments or markets where concentrations exist. FIs should consider also "worst case" scenarios in addition to more probable events.

Further, the BSP will expect FIs with material market risk exposure, particularly from derivatives and/or structured products to supplement their stress testing with an analysis of their exposure to "interconnection risk." While stress testing typically considers the movement of a single market factor (e.g., interest rates), interconnection risk considers the linkages across markets (e.g., interest rates and foreign exchange rates) and across the various categories of risk (e.g., credit, and liquidity risk). For example, stress from one market may transmit shocks to other markets and give rise to otherwise dormant risks, such as liquidity risk. Evaluating interconnected risk involves assessing the total or aggregate impact of singular events.

Guidelines for performing stress testing should be detailed in the risk management policy statement. Management and the board of directors should periodically review the design, major assumptions, and the results of such stress tests to ensure that appropriate contingency plans are in place.

(3) Model output. Reports should be provided to senior management and the Board as a basis for making decisions. Report content should be clear and straightforward, indicating the purpose of the model, significant limitations, the quantitative level of risk estimated by the

simulation, a comparison to Board approved limits and a qualitative discussion regarding the appropriateness of the FI's current exposures. Sophisticated simulations should be used carefully so that they do not become "black boxes" producing numbers that have the appearance of precision but may not be very accurate when their specific assumptions and parameters are revealed.

Market limits structure

The FI's board of directors should set the institution's tolerance for market risk and communicate that tolerance to senior management. Based on these tolerances, senior management should establish appropriate risk limits, duly approved by the Board, to maintain the FI's exposure within the set tolerances over a range of possible changes in market risk factors such as interest rates.

Limits represent the FI's actual willingness and ability to accept real losses. In setting risk limits, the board and senior management should consider the nature of the FI's strategies and activities, past performance, and management skills. Most importantly, the board and senior management should consider the level of the FI's earnings and capital and ensure that both are sufficient to absorb losses equal to the proposed limits. Limits should be approved by the board of directors. Furthermore, limits should be flexible to changes in conditions or risk tolerances and should be reviewed periodically.

An FI's limits should be consistent with its overall approach to measuring market risk. At a minimum, FIs using simple gap should establish limits on mismatches in each time bucket on a stand-alone and cumulative basis. In addition, limits should be adopted to control potential losses in the investment portfolio to a pre-set percentage of capital.

Larger, more complex FIs should establish limits on the potential impact of changes in market risk factors on reported earnings and/or the FI's economic value of equity. Market risk limits may include limits on net and gross positions, volume limits, stop-loss limits, value-at-risk limits, re-pricing gap limits, earnings-at-risk limits and other limits that capture either notional or (un)expected loss exposures. In assigning interest rate risk limits under the earnings perspective, FIs should explore limits on the variability of net income as well as net interest income in order to fully assess the contribution of non-interest income to the interest rate risk exposure of the FI. Such limits usually specify acceptable levels of earnings volatility under specified interest rate scenarios.

For example, interest rate risk limits may be keyed to specific scenarios of movements in market interest rates such as an increase or decrease of a particular magnitude. The rate movements used in developing these limits should represent meaningful stress situations taking into account historic rate volatility and the time required for management to address exposures. Limits may also be based on measures derived from the underlying statistical distribution of interest rates, such as earnings at risk or economic value-at-risk techniques. Moreover, specified scenarios should take account of the full range of possible sources of interest rate risk to the FI including re-pricing, yield curve, basis, and option risks. Simple scenarios using parallel shifts in interest rates may be insufficient to identify such risks. This is particularly important for FIs with significant exposures to these sources of market risk.

The form of limits for addressing the effect of rates on an FI's economic value of equity should be appropriate for the size and complexity of its underlying positions. For FIs engaged in traditional banking

activities, relatively simple limits may suffice. However, for FIs with significant holdings of long-term instruments, options, instruments with embedded options, or other structured instruments, more detailed limit systems may be required.

Depending on the nature of an FI's holdings and its general sophistication, limits can also be identified for individual business units, portfolios, instrument types, or specific instruments. The level of detail of risk limits should reflect the characteristics of the FI's holdings including the various sources of market risk the FI is exposed to.

The BSP also expects that the limits system will ensure that positions that exceed predetermined levels receive prompt management attention. Limit exceptions should be communicated to appropriate senior management without delay. Policies should include how senior management will be informed and what action should be taken by management in such cases. Particularly important is whether limits are absolute in the sense that they should never be exceeded or whether, under specific circumstances, breaches of limits can be tolerated for a short period of time. The circumstances leading to a tolerance of breaches should be clearly described.

Market risk monitoring and reporting

An accurate, informative, and timely management information system is essential for managing market risk exposures both to inform management and to support compliance with board policy. Reporting of risk measures should be done regularly and should clearly compare current exposure to policy limits. In addition, past forecasts or risk estimates should be compared with actual results to identify any modeling shortcomings.

Reports detailing the market risk exposure of the FI should be reviewed by the board on a regular basis. While the types of reports prepared for the board and for various levels of management will vary based on the FI's market risk profile, they should at a minimum include the following:

1. Summaries of the FI's aggregate exposures;
2. Reports demonstrating the FI's compliance with policies and limits;
3. Summary of key assumptions, for example, non-maturity deposit behavior, prepayment information, and correlation assumptions;
4. Results of stress tests, including those assessing breakdowns in key assumptions and parameters; and
5. Summaries of the findings of reviews of market risk policies, procedures, and the adequacy of the market risk measurement systems, including any findings of internal and external auditors and retained consultants.

D. Risk controls and audit

Adequate internal controls ensure the integrity of an FI's market risk management process. These internal controls should be an integral part of the institution's overall system of internal control and should promote effective and efficient operations, reliable financial and regulatory reporting, and compliance with relevant laws, regulations, and institutional policies. An effective system of internal control for market risk includes:

1. A strong control environment;
2. An adequate process for identifying and evaluating risk;
3. The establishment of control activities such as policies, procedures, and methodologies;
4. Adequate information systems;
5. Continual review of adherence to established policies and procedures; and
6. An effective internal audit and independent validation process.

Policies and procedures should specify the approval processes, exposure limits, reconciliations, reviews, and other control mechanisms designed to provide a reasonable assurance that the institution's market risk management objectives are achieved. Many attributes of a sound risk management process, including risk measurement, monitoring, and control functions, are actually key aspects of an effective system of internal control. FIs should ensure that all aspects of the internal control system are effective, including those aspects that are not directly part of the risk management process.

An important element of an FI's internal control system is regular evaluation and review. The BSP expects that FIs will establish a process to ensure that its personnel are following established policies and procedures, and that its procedures are actually accomplishing their intended objectives. Such reviews and evaluations should also address any significant change that may impact the effectiveness of controls, and that appropriate follow-up action was implemented when limits were breached. Management should ensure that all such reviews and evaluations are conducted regularly by individuals who are independent of the function they are assigned to review. When revisions or enhancements to internal controls are warranted, there should be a mechanism in place to ensure that these are implemented in a timely manner.

Independent reviews of the market risk measurement system should also include assessments of the assumptions, parameters, and methodologies used. Such reviews should seek to understand, test, and document the current measurement process, evaluate the system's accuracy, and recommend solutions to any identified weaknesses. If the measurement system incorporates one or more subsidiary systems or processes, the review should include testing aimed at ensuring that the subsidiary systems are well-integrated and consistent with each other in all critical respects. The results of this review, along with any recommendations for improvement, should be reported to senior management and/or the board.

The BSP expects that FIs with complex risk exposures should have their measurement, monitoring, and control functions reviewed on a regular basis by an independent party (such as an internal or external auditor). In such cases, reports written by external auditors or other outside parties should be available to the BSP. It is essential that any independent reviewer ensures that the FI's risk measurement system is sufficient to capture all material elements of market risk, whether arising from on- or off-balance-sheet activities. Among the items that an audit should review and validate are:

1. The appropriateness of the FI's risk measurement system(s) given the nature, scope, and complexity of its activities.

2. The accuracy and completeness of the data inputs - This includes verifying that balances and contractual terms are correctly specified and that all major instruments, portfolios, and business units are captured in the model. The review should also investigate whether data extracts and model inputs have been reconciled with transactions and general ledger systems.[1]

3. The reasonableness and validity of scenarios and assumptions – This includes a review of the appropriateness of the

[1] It is acceptable for parts of the reconciliation to be automated; e.g., routines may be programmed to investigate whether the balances being extracted from various transaction systems match the balances recorded on the FI's general ledger. Similarly, the model itself often contains various audit checks to ensure, for example, that maturing balances do not exceed original balances.

interest rate scenarios as well as customer behaviors and pricing/volume relationships to ensure that these assumptions are reasonable and internally consistent.[1]

4. The validity of the risk measurement calculations - The scope and formality of the measurement validation will depend on the size and complexity of the FI. At large FIs, internal and external auditors may have their own models against which the FI's model is tested. FIs with more complex risk profiles and measurement systems should have the model or calculations audited or validated by an independent source. At smaller and less complex FIs, periodic comparisons of actual performance with forecasts may be sufficient.[2]

The frequency and extent to which an FI should re-evaluate its risk measurement methodologies and models depend, in part, on the particular market risk exposures created by holdings and activities, the pace and nature of market rate changes, and the pace and complexity of innovation with respect to measuring and managing market risk.

VI. Capital adequacy

In addition to adequate risk management systems and controls, capital has an important role to play in mitigating and supporting market risk. FIs must hold capital commensurate with the level of market risk they undertake. As part of sound market risk management, FIs must translate the level of market risk they undertake whether as part of their trading or non-trading activities, into their overall evaluation of capital adequacy. Where market risk is undertaken as part of an FI's trading activities, existing capital adequacy ratio requirements shall prevail.

The BSP will periodically evaluate the market risk measurement system for the accrual book to determine if the FI's capital is adequate to support its exposure to market risk and whether the internal measurement systems of the FI are adequate. In performing this assessment, the BSP may require information regarding the market risk exposure of the FI, including re-pricing gaps, earnings and economic value simulation estimates, and the results of stress tests. This information will typically be found in internal management reports.

If an FI's internal measurement system does not adequately capture the level of market risk, the BSP may require an FI to improve its system. In cases where an FI accepts significant market risk in its accrual book, the BSP expects that a portion of capital will be allocated to cover this risk.

When performing these evaluations, the BSP will determine if:

(a) All material market risk associated with an institution's assets, liabilities, and off-balance sheet positions in the accrual book are captured by the risk management systems;

(b) Generally accepted financial concepts and risk measurement techniques are utilized. For larger, complex FIs, internal systems must be capable of measuring risk using both an earnings and economic value approach.

(c) Data inputs are adequately specified (commensurate with the nature

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[1] Key areas of review include the statistical methods that were used to generate scenarios and assumptions (if applicable), and whether senior management reviewed and approved key assumptions. The review should also compare actual pricing spreads and balance sheet behavior to model assumptions. For some instruments, estimates of value changes can be compared with market value changes. Unfavorable results may lead the FI to revise model relationships.

[2] The validity of the model calculations is often tested by comparing actual with forecasted results. When doing so, FIs can compare projected net income results with actual earnings. Reconciling the results of economic valuation systems can be more difficult because market prices for all instruments are not always readily available, and the FI does not routinely mark all of its balance sheet to market. For instruments or portfolios with market prices, these prices are often used to benchmark or check model assumptions.

and complexity of an FI's holdings) with regard to rates, maturities, re-pricing, embedded options, and other details;

(d) The system's assumptions (used to transform positions into cash flows) are reasonable, properly documented, and stable over time.[1]

(e) Market risk measurement systems are integrated into the institution's daily risk management practices. The output of the systems should be used in characterizing the level of market risk to senior management and board of directors.

(Circular No. 544 dated 15 September 2006)

[1] This is especially important for assets and liabilities whose behavior differs markedly from contractual maturity or re-pricing, and for new products. Material changes to assumptions should be documented, justified, and approved by management.

GUIDELINES ON LIQUIDITY RISK MANAGEMENT

[Appendix to Sec. 4175Q (2008 - 4195Q), 4195S, 4195P and 4195N]

I. Background

The on-going viability of institutions, particularly financial organizations, is heavily influenced by their ability to manage liquidity. Innovations in investment and funding products, growth in off-balance sheet activities and continuous competition for consumer funds have affected the way FI do business and intensified the need for proactive liquidity risk management. FIs need to fully understand, measure and control the resulting liquidity risk exposures.

II. Statement of Policy

For purposes of these guidelines, FIs include banks, NBFIs supervised by the BSP and their financial subsidiaries.

The BSP recognizes the liquidity risk inherent in FI activities and how these activities expose an FI to multiple risks which may increase liquidity risk. The BSP will not restrict risk-taking activities as long as FIs are authorized to engage in such activities and:

1. Understand, measure, monitor and control the risk they assume;
2. Adopt risk management practices whose sophistication and effectiveness is commensurate to the risk assumed; and
3. Maintain capital commensurate with their risk exposures.

The principles set forth in these guidelines shall be used to determine the level and trend of liquidity risk exposure and adequacy and effectiveness of an FI's liquidity risk management process. In evaluating the adequacy of an FI's liquidity position, the BSP shall consider the FI's current level and prospective sources of liquidity as compared to its funding needs. Further, the BSP will evaluate the adequacy of funds management practices relative to the FI's size, complexity, and risk profile.

In general, liquidity risk management practices should ensure that an institution is able to maintain a level of liquidity sufficient to meet its financial obligations in a timely manner and to fulfill the legitimate funding needs of its community. Practices should reflect the ability of the institution to manage unplanned changes in funding sources, as well as react to changes in market conditions that affect the ability to quickly liquidate assets with minimal loss. In addition, funds-management practices should ensure that liquidity is not consistently maintained at a high cost, from concentrated sources, or through undue reliance on funding sources that may not be available in times of financial stress or adverse changes in market conditions.

In evaluating the above parameters, the BSP shall consider the following factors:

1. The actual and potential level of liquidity risk posed by the FI's products and services, balance sheet structure and off-balance sheet activities;
2. The cost of an FI's access to money markets and other alternative sources of funding;
3. The diversification of funding sources (on and off-balance sheet);
4. The adequacy and effectiveness of board and senior management oversight, particularly the Board's ability to recognize the effects of interrelated risk areas, such as market and reputation risks, to liquidity risk;
5. The reasonableness of liquidity risk limits and controls in relation to earnings, as affected by the cost of access to money markets and other alternative sources of funding, and capital;

6. The adequacy of measurement methodologies, monitoring and management information systems;

7. The adequacy of foreign currency liquidity management;

8. The appropriateness and reasonableness of contingency plans for handling liquidity crises;

9. The adequacy of internal controls and audit of liquidity risk management process.

The sophistication of liquidity risk management shall depend on the size, nature and complexity of an FI's activities. However, in all instances, FIs are expected to measure their liquidity position on an ongoing basis, analyze net funding requirements under alternative scenarios, diversify funding sources and adopt contingency funding plans.

An FI's liquidity risk management system shall be assessed under the FI's general risk management framework, consistent with the guidelines on supervision by risk as set forth under *Appendix Q-42*. If an FI's risk exposures are deemed excessive relative to the FI's capital, or that the risk assumed is not well managed, the BSP will direct the FI to reduce its exposure and/or strengthen its risk management system.

III. Liquidity Risk Management Process

Liquidity risk management process should be tailored to an FI's structure and scope of operations and application can vary across institutions. Regardless of the structure, an FI's liquidity risk management process should be consistent with its general risk management framework and should be commensurate with the level of risk assumed. At a minimum, the process should:

1. *Identify liquidity risk*. Proper identification of liquidity risk requires that management understand both existing risk and prospective risks from new products and activities. It involves determining the volume and trends of liquidity needs and the sources of liquidity available to meet these needs. Identifying liquidity risk necessitates expressing the FI's desired level of risk exposure based on its ability and willingness to assume risk which may primarily depend on the FI's capital base and access to funds providers. Liquidity risk identification should be a continuing process and should occur at both the transaction, portfolio and entity level.

2. *Measure liquidity risk***.** Adequate measurement systems enable FIs to quantify liquidity risk exposures on a per entity basis and across the consolidated organization. A relatively large organization with extensive scope of operations would generally require a more robust management information system to properly measure risk in a timely and comprehensive manner.

3. *Control liquidity risk*. The FI should establish policies and standards on acceptable product types, activities, counterparties and set risk limits on a transactional, portfolio and aggregate/ consolidated basis to control liquidity risk. In setting limits, the FI should recognize any legal distinctions and possible obstacles to cash flow movements among affiliates or across separate books. Lines of authority and accountability should be clearly defined to ensure liquidity risk exposures remain reasonable and within the risk tolerance expressed by the board.

4. *Monitor liquidity risk***.** Monitoring liquidity risk requires timely review of liquidity risk positions and exceptions, including day-to-day liquidity management. Monitoring reports should be frequent, timely, and accurate and should be distributed to appropriate levels of management.

IV. Definition of Liquidity Risk

Liquidity risk is generally defined as the current and prospective risk to earnings or capital arising from an FI's inability to meet its obligations when they come due without incurring unacceptable losses or costs. Liquidity risk includes the inability to manage unplanned decreases or changes in funding sources. Liquidity risk also arises from the failure to recognize or address changes in market conditions that affect the ability to liquidate assets quickly and with minimal loss in value.

In terms of capital markets and trading activities, FIs face two (2) types of liquidity risk: *funding liquidity risk* and *market liquidity risk*. *Funding liquidity risk* refers to the inability to meet investment and funding requirements arising from cash flow mismatches without incurring unacceptable losses or costs. This is synonymous with the general definition of liquidity risk.

Market liquidity risk, on the other hand, refers to the risk that an institution cannot easily eliminate or offset a particular position because of inadequate liquidity in the market. The size of the bid/ask spread of instruments in a market provides a general indication of its depth, hence its liquidity, under normal circumstances. Market liquidity risk is also associated with the probability that large transactions may have a significant effect on market prices in markets that lack sufficient depth. In addition, market liquidity risk is associated with structured or complex investments as the market of potential buyers is typically small. Finally, FIs are exposed to the risk of an unexpected and sudden erosion of market liquidity. This could be the result of sharp price movement or jump in volatility, or internal to the FI such as that posed by a general loss of market confidence. Understanding market liquidity risk is particularly important for institutions with significant holdings of instruments traded in financial markets.

Market and liquidity risks are highly interrelated, particularly during times of uncertainty when there is a high correlation between the need for liquidity and market volatility. Likewise, an FI's exposure to other risks such as reputation, strategic, and credit risks, can likewise significantly affect an institution's liquidity risk. It is therefore important that an FI's liquidity risk management system is consistent with its general risk management framework.

V. Sound Liquidity Risk Management Practices

When assessing an FI's liquidity risk management system, the BSP shall consider how an FI address the four basic elements of a sound risk management system:

1. Active and appropriate board and senior management oversight;
2. Adequate risk management policies and procedures;
3. Appropriate risk measurement methodologies, limits structure, monitoring and management information system; and
4. Comprehensive internal controls and independent audits

Evaluation of the adequacy of the FI's application of the above elements will be relative to the FI's risk profile. FIs with less complex operations may generally use more basic practices while larger, and/or more complex institutions will be expected to adopt more formal and sophisticated practices. Large organizations should likewise take a comprehensive perspective to measuring and controlling liquidity risk by understanding how subsidiaries and affiliates can raise or lower the consolidated risk profile.

APP. Q-44
08.12.31

A. Active and Appropriate Board and Senior Management Oversight[1]

Effective liquidity risk management requires that the Board and senior management be fully informed of the level of liquidity risk assumed by the FI and ensure that the activities undertaken are within the prescribed risk tolerance. Senior management should have a thorough understanding of how other risks such as credit, market, operational and reputation risks impact the FI's overall liquidity strategy.[1]

Responsibilities of the board of directors

The Board has the ultimate responsibility for understanding the nature and level of liquidity risk assumed by the FI and the processes used to manage it.

The board of directors should:

1. Establish and guide the FI's strategic direction and tolerance for liquidity risk by adopting a formal written liquidity/funding policy that specifies quantitative and qualitative targets;
2. Approve policies that govern or influence the FI's liquidity risk, including reasonable risk limits and clear guidelines which are adequately documented and communicated to all concerned;
3. Identify the Senior Management staff who has the authority and responsibility for managing liquidity risk and ensure that this staff takes the necessary steps to monitor and control liquidity risk;
4. Monitor the FI's performance and overall liquidity risk profile in a timely manner by requiring frequent reports that outline the liquidity position of the FI along with information sufficient to determine if the FI is complying with established risk limits;
5. Mandate and track the implementation of corrective action in instances of breaches in policies and procedures;
6. Establish, review and to the extent possible, test contingency plans for dealing with potential temporary and long-term liquidity disruptions; and
7. Ensure that the FI has sufficient competent personnel, including internal audit staff, and adequate measurement systems to effectively manage liquidity risk.

Responsibilities of senior management

Senior management is responsible for effectively executing the liquidity strategy and overseeing the daily and long-term management of liquidity risk. In managing the FI's activities, Senior Management should:

1. Develop and implement procedures and practices that translate the Board's goals, objectives, and risk tolerances into operating standards that are transmitted to and well understood by personnel. Operating standards should be consistent with the Board's intent;
2. Plan for adequate sources of liquidity to meet current and potential funding needs and establish guidelines for the development of contingency funding plans;
3. Adhere to the lines of authority and responsibility that the Board has established for managing liquidity risk;
4. Oversee the implementation and maintenance of management information and other systems that identify, measure, monitor, and control the FI's liquidity risk; and
5. Establish effective internal controls over the liquidity risk management process.

In evaluating the quality of oversight provided by the Board and Senior

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[1] This section refers to a management structure composed of a board of directors and senior management. The BSP is aware that there may be differences in some FIs as regards the organizational framework and functions of the board of directors and senior management. For instance, branches of foreign banks have board of directors located outside of the Philippines and are overseeing multiple branches in various countries. In this case, "board-equivalent" committees are appointed. Owing to these differences, the notions of the board of directors and the senior management are used in these guidelines not to identify legal constructs but rather to label two decision-making functions within a FI.

Management, the BSP will evaluate how the Board and Senior Management carry out the above functions/responsibilities. Further, sound management practices are highly related to the quality of other areas/ elements of risk management system. Thus, even if Board and Senior Management exhibit active oversight, the FI's policies, procedures, measurement methodologies, limits structure, monitoring and information systems, controls and audit should be adequate before quality of Board and Senior Management can be considered "satisfactory".

Lines of Responsibility and Authority

Management of liquidity risk generally requires collaboration from various business areas of the FI, thus a clear delineation of responsibilities is necessary. The management structure should clearly define the duties of senior level committees, members of which have authority over the units responsible for executing liquidity-related transactions. There should be a clear delegation of day-to-day operating responsibilities to particular departments such as the Treasury Department.

To ensure proper management of liquidity risk, the FI should designate an independent unit responsible for measuring, monitoring and controlling liquidity risk. Said unit should take a comprehensive approach and directly report to the board of directors or a committee thereof.

B. Adequate risk management policies and procedures

An FI's liquidity risk policies and procedures should be comprehensive, clearly defined, documented and duly approved by the board of directors. Policies and procedures should cover the FI's liquidity risk management system in order to provide appropriate guidance to management. These policies should be applied on a consolidated basis and, as appropriate, at the level of individual affiliates, especially when recognizing legal distinctions and possible obstacles to cash movements among affiliates.

Liquidity risk policies should identify the quantitative parameters used by the FI to define the acceptable level of liquidity risk such as risk limits and financial ratios as well as describe the measurement tools and assumptions used. Qualitative guidelines should include description of the FI's acceptable products and activities, including off-balance sheet transactions, desired composition of assets and liabilities, and approach towards managing liquidity in different currencies, geographies and across subsidiaries and affiliates. Where appropriate, a large FI should apply these policies on a consolidated basis to address risk exposures resulting from inter-connected funding structures and operations among members of an FI's corporate group.

It is essential that policies include the development of a formal liquidity risk measurement system that addresses business-as-usual scenarios and a contingency funding plan that addresses a variety of stress scenarios. FIs should likewise have specific procedures for addressing breaches in policies and implementation of corrective actions.

Management should periodically review its liquidity risk policies and ensure that these remain consistent with the level and complexity of the FI's operations. Policies should be updated to incorporate effects of new products/activities, changes in corporate structure and in light of its liquidity experience.

C. Appropriate risk measurement methodologies, limits structure, monitoring, and management information system

Liquidity risk measurement models/ methodologies

An FI should have a measurement system in place capable of quantifying and capturing the main sources of liquidity risk in a timely and comprehensive manner. Liquidity management requires ongoing measurement, from intra-day liquidity to long-term liquidity positions. Depending on its risk profile, an FI can use techniques of simple calculations, static simulations based on current holdings or sophisticated models. What is essential is that the FI should be able to identify and avoid potential funding shortfalls such that the FI can consistently meet investment, funding and/or strategic targets.

FIs with simple operations can generally use a static approach to liquidity management. Static models are based on positions at a given point in time. While an exact definition of "simple operations" will not be provided, the BSP expects that banks using a static approach to liquidity management would limit their operations to core banking activities such as accepting plain vanilla deposits and making traditional loans. Such banks would not have active Treasury Departments, would not hold or offer structured products and would not be exposed to significant levels of FX risk. Board reporting could be less frequent than in more complex banks but in no event should be less than quarterly.

Complex FIs, on the other hand, will be expected to adopt more robust approaches such as a dynamic maturity/ liquidity gap reporting or even simulation modeling. At a minimum, universal banks should use maximum cash outflow/ liquidity or maturity gap models. FIs engaged in holding or offering significant levels of structured products and/or derivatives will be expected to have the capability to model the cash flows from these instruments under a variety of scenarios. Specifically, scenarios should be designed to measure the effects of a breach of the triggers (strike price) on these instruments.

Where the FI's organizational structure and business practices indicate cash flow movements and liquidity support among corporate group members, the FI should adopt consolidated risk measurement tools to help management assess the group's liquidity risk exposure. Depending on the degree of inter-related funding, non-complex measurement and monitoring systems may be acceptable. However, large, complex FIs that display a high degree of inter-related and inter-dependent funding will be expected to utilize more sophisticated monitoring and management systems. These systems should enable the Board of the consolidated entity to simulate and anticipate the funding needs of the FIs on both a consolidated basis and in each of its component parts.

Liquidity risk measurement methodologies/models should be documented and approved by the board and should be periodically independently reviewed for reasonableness and tested for accuracy and data integrity. Assumptions used in managing liquidity should be periodically revisited to ensure that these remain valid.

Liquidity models require projecting all relevant cash flows. As such, FIs engaged in complex activities should have the capability to model the behavior of all assets, liabilities, and off-balance sheet items both under normal/business-as usual and a variety of stressed conditions. Stressed conditions may include liquidity crisis confined within the institution, or a systemic liquidity crisis, in which all FIs are affected. For FIs operating in a global environment, cash flow projections should reflect various foreign-currency funding requirements.

When projecting cash flows, management should also estimate

customer behavior in addition to contractual maturities. Many cash flows are uncertain and may not necessarily follow contractual maturities. Cash flows may be influenced by interest rates and customer behavior, or may simply follow a seasonal or cyclical pattern. When modeling liquidity risk, it is important that assumptions be documented. Assumptions should be reasonable and should be based on past experiences or with consideration of the potential impact of changes in business strategies and market conditions. Measurement tools should include a sufficient number of time bands to enable effective monitoring of both short- and long-term exposures. This expectation applies not only to complex simulation modeling, but to the construction of simple liquidity GAP models as well.

To sufficiently measure an FI's liquidity risk, management should analyze how its liquidity position is affected by changes in internal (company-specific) and external (market-related) conditions. Management will need to assess how a shift from a normal scenario to various levels of liquidity crisis can affect its ability to source external funds and at what cost, liquidate certain assets at expected prices within expected timeframes, or hasten the need to settle obligations (e.g., limited ability to roll-over deposits). Management should, at a minimum, consider stress scenarios where securities are sold at prices lower than anticipated and credit lines are partially or wholly cancelled.

Regardless of the liquidity risk models used, an FI should adopt an appropriate contingency plan for handling liquidity crisis. Well before a liquidity crisis occurs, management should carefully plan how to handle administrative matters in a crisis. Management credibility, which is essential to maintaining the public's confidence and access to funding, can be gained or lost depending on how well or poorly some administrative matters are handled. A contingency funding/liquidity plan ensures that an FI is ready to respond to liquidity crisis.

The sophistication of a contingency plan should be commensurate with the FI's complexity and risk exposure, activities, products and organizational structure. The plan should identify the types of events that will trigger the contingency plan, quantify potential funding needs and sources and provide the specific administrative policies and procedures to be followed in a liquidity crisis.

Specifically, the contingency plan should:

1. Clearly identify, quantify and rank all sources of funding by preference including, but not limited to:
   - Reducing assets
   - Modifying the liability structure or increasing liabilities
   - Using off-balance-sheet sources, such as securitizations
   - Using other alternatives for controlling balance sheet changes
2. Consider asset and liability strategies for responding to liquidity crisis including, but not limited to:
   - Whether to liquidate surplus money market assets
   - When (if at all) HTM securities might be liquidated
   - Whether to sell liquid securities in the repo markets
   - When to sell longer-term assets, fixed assets, or certain lines of business
   - Coordinating lead bank funding with that of the FI's other banks and non-bank affiliates
   - Developing strategies on how to interact with non-traditional funding sources (e.g., whom to contact, what type of information and how much detail should be provided, who will be available for further questions, and how to ensure that communications are consistent)

3. Address administrative policies and procedures that should be used during a liquidity crisis:

- The responsibilities of Senior Management during a funding crisis
- Names, addresses, and telephone numbers of members of the crisis team
- Where, geographically, team members will be assigned
- Who will be assigned responsibility to initiate external contacts with regulators, analysts, investors, external auditors, press, significant customers, and others
- How internal communications will flow between management, Asset Liability Committee (ALCO), investment portfolio managers, traders, employees, and others
- How to ensure that the ALCO receives management reports that are pertinent and timely enough to allow members to understand the severity of the FI's circumstances and to implement appropriate responses.

The above outline of the scope of a good contingency plan is by no means exhaustive. FIs should devote significant time and consideration to scenarios that are most likely, given their activities. Regardless of the strategies employed, an FI should consider the effects of such strategies on long-term liquidity positions and take appropriate actions to ensure that level of risk exposures shall remain or be brought down within the risk tolerance of the Board.

Limits structure

The board and senior management should establish limits on the nature and amount of liquidity risk they are willing to assume. In setting limits, management should consider the nature of the FI's strategies and activities, its past performance, the level of earnings and capital available to absorb potential losses and costs of an FI's access to money markets and other alternative sources of funding.

Limits can take various forms. FIs should address limits on types of funding sources and uses of funds, including off-balance sheet positions. In addition, policies should set targets for minimum holdings of liquid assets relative to liabilities. Complex FIs, or FIs engaged in complex activities should set maximum cumulative cash-flow mismatches over particular time horizons and establish counterparty limits. Such limits should be applied to all currencies to which the FI has a significant exposure. In particular, FIs should take into consideration any legal distinctions and possible obstacles to cash flow movements between the Regular Banking Unit (RBU) and the FCDU.

When evaluating a bank's liquidity position, the BSP will consider low levels of liquid assets relative to liabilities, and significant negative funding gaps to be indicative of high liquidity risk exposure. Further, negative cash-flow mismatches in the short term time buckets will receive heightened scrutiny by the BSP and should also receive the attention of senior management and the board of directors.

Before accepting negative funding gaps, or setting limits that allow negative funding gaps, the board and senior management should consider the FI's ability to fund these negative gaps. Factors include, but are not limited to: the availability of on-balance sheet liquidity, the amount of firm credit lines available from commercial sources that can be drawn to fund the shortfall, and the amount of unencumbered on-balance sheet assets that can be sold without excessive loss and in a reasonable time-frame.

Further, actual positions and limits should reflect the outcome of possible stress scenarios caused by internal and external factors, particularly those related to reputation risk. Stress scenarios should consider the possibility that securities may be sold at a greater discount and/or may take more time to sell than expected or

that credit lines and other off-balance sheet sources of funding may be cancelled or may be unavailable at reasonable cost.

Management should define specific procedures for the prompt reporting and documentation of limit exceptions and the management approval and action required in such cases.

Liquidity risk monitoring and reporting

An adequate management information system is critical in the risk monitoring process. The system should be able to provide the Board, senior management and other personnel with timely information on the FI's liquidity position in all the major currencies it deals in, on an individual and aggregate basis, and for various time periods.

Effective liquidity risk monitoring requires frequent routine liquidity reviews and more in-depth and comprehensive reviews on a periodic basis. In general, monitoring should include sufficient information and a clear presentation such that the reader can determine the FI's ongoing degree of compliance with risk limits. For example, reports should address funding concentrations, funding costs, projected funding needs and available funding sources.

Monitoring and board reporting should be robust. It is not unreasonable to expect complex FIs or FIs engaged in complex activities to monitor liquidity on a daily basis. Board reporting should be no less frequent than monthly. However, the BSP would expect Board-level committees or sub-committees to receive more frequent reporting.

Comprehensive and accurate internal reports analyzing an FI's liquidity risk should be regularly prepared and reviewed by senior management and submitted to the board of directors.

D. Risk controls and audit

An FI should have adequate internal controls in place to protect the integrity of its liquidity risk management process. Fundamental to the internal control system is for the Board to prescribe independent reviews to evaluate the effectiveness of the risk management system and check compliance with established limits, policies and procedures.

An effective system of internal controls for liquidity risk includes:

1. A strong internal control environment;
2. An adequate process for identifying and evaluating liquidity risk;
3. Adequate information systems; and
4. Continual review of adherence to established policies and procedures.

To ensure that risk management objectives are achieved, management needs to focus on the following areas: appropriate approval processes, limits monitoring, periodic reporting, segregation of duties, restricted access to information systems and the regular evaluation and review by independent competent personnel.

Internal audit reviews should cover all aspects of the liquidity risk management process, including determining the appropriateness of the risk management system, accuracy and completeness of measurement models, reasonableness of assumptions and stress testing methodology. Audit staff should have the skills commensurate with the sophistication of the FI's risk management systems. Audit results should be promptly reported to the board. Deficiencies should be addressed in a timely manner and monitored until resolved/corrected.

E. Foreign currency liquidity management

The principles described in this Appendix also apply to the management

of any foreign currency to which the FI maintains a significant exposure. Specifically, management should ensure that its measurement, monitoring and control systems account for these exposures as well. Management needs to set and regularly review limits on the size of its cash flow mismatches for each significant individual currency and in aggregate over appropriate time horizons. In addition, an FI should consider effects of other risk areas, particularly settlement risks from its off-balance sheet activities. An FI should also conservatively assess its access to foreign exchange markets when setting up its risk limits. As with overall liquidity risk management, foreign currency liquidity should be analyzed under various scenarios, including stressful conditions.

(Circular No. 545 dated 15 September 2006)

AUTHORIZATION FORM FOR QUERYING THE BANGKO SENTRAL WATCHLIST FILES FOR SCREENING APPLICANTS AND CONFIRMING APPOINTMENTS OF DIRECTORS AND OFFICIALS

(Appendix to Subsecs. 4143Q.5, 4143S.6, 4143P.6 and 4143N.6)

AUTHORIZATION

I, _____, after being sworn in accordance with law, do hereby authorize the following, pursuant to the provisions of Subsecs. 4143Q.5(c), 4143S.6(c), 4143P.6(c) and 4143N.6(c) of the MORNBFI:

a) _____(Name of NBFI)_____ to conduct a background investigation on myself relative to my application for or appointment to the position of (position) in (Name of NBFI) which include, among others, inquiring from the Watchlist Files of the BSP; and

b) The BSP to disclose its findings pertinent to the aforementioned inquiry on the said watchlist files to ___(Name of NBFI)_____.

With the above authorization, I hereby waive my right to the confidentiality of the information that will be obtained as a result of the said inquiry, provided that disclosure of said information will be limited for the purpose of ascertaining my qualification or non-qualification for the said position.

IN WITNESS WHEREOF, I have hereunto set my hand this _____.

_____
(Signature Over Printed Name)

SIGNED IN THE PRESENCE OF:

_____ _____
(Witness) (Witness)

APP. Q-45
08.12.31

ACKNOWLEDGMENT

REPUBLIC OF THE PHILIPPINES } S.S.
_____CITY }

BEFORE ME, this ___ day of _____200___ in _____ personally appeared the following person:

Name	Community Tax Certificate	Place	Date

known to me to be the same person who executed the foregoing instrument and he acknowledged to me to be the same person who executed the foregoing instrument and he acknowledged to me that the same is his free act and deed.

This instrument, consisting of two (2) pages, including the page on which this acknowledgment is written, has been signed on the left margin of each and every page thereof by _____, and his witnesses, and sealed with my notarial seal.

IN WITNESS WHEREOF, I have hereunto set my hand, the day, year and place above written.

Notary Public

Doc. No.: _____
Page No.: _____
Book No.: _____
Series of 200___

(As amended by CL-2007-001 dated 04 January 2007 and CL-2006-046 dated 21 December 2006)

RISK-BASED CAPITAL ADEQUACY FRAMEWORK FOR THE PHILIPPINE BANKING SYSTEM

[Appendix to Sec. 4115Q (2008 - 4116Q)]

Introduction

This Appendix outlines the BSP implementing guidelines of the revised *International Convergence of Capital Measurement and Capital Standards*, or popularly known as Basel II. Basel II is the new international capital standards set by the Basel Committee on Banking Supervision (BCBS)[1]. It aims to replace Basel I, which was issued in 1988 with an amendment in 1996, to make the risk-based capital framework more risk-sensitive. Banks are enjoined to submit their group-wide (including subsidiary banks and QBs) Basel II implementation plans from 2007-2010, not later than 31 December 2006.

The guidelines contained in this Appendix shall take effect on 01 July 2007.
(As amended by M-2006-022 dated 24 November 2006)

Part I. Risk-based capital adequacy ratio

1. The risk-based CAR of UBs and KBs and their subsidiary banks and QBs, expressed as a percentage of qualifying capital to risk-weighted assets, shall not be less than ten percent (10%).

2. Qualifying capital is computed in accordance with the provisions of Part II. Risk-weighted assets is the sum of (1) credit risk-weighted assets (Parts III, IV, and V), (2) market risk-weighted assets (Parts IV and VI), and (3) operational risk-weighted assets (Part VII).

3. The CAR requirement will be applied to all UBs and KBs and their subsidiary banks, and QBs on both solo and consolidated bases. The application of the requirement on a consolidated basis is the best means to preserve the integrity of capital in banks with subsidiaries by eliminating double gearing. However, as one of the principal objectives of supervision is the protection of depositors, it is essential to ensure that capital recognized in capital adequacy measures is readily available for those depositors. Accordingly, individual banks should likewise be adequately capitalized on a stand-alone basis.

4. To the greatest extent possible, all banking and other relevant financial activities (both regulated and unregulated) conducted by a bank and its subsidiaries will be captured through consolidation. Thus, majority-owned or -controlled financial allied undertakings should be fully consolidated on a line by line basis. Exemptions from consolidation shall only be made in cases where such holdings are acquired through debt previously contracted and held on a temporary basis, are subject to different regulation, or where non-consolidation for regulatory capital purposes is otherwise required by law. All cases of exemption from consolidation must be made with prior clearance from the BSP.

5. Banks shall comply with the minimum CAR at all times notwithstanding that supervisory reporting shall only be on quarterly basis. Any breach, even if only temporary, shall be reported to the bank's Board of Directors and to BSP, SES within three (3) banking days. For this purpose, banks shall develop an appropriate system to properly monitor their compliance.

6. The BSP reserves the right, upon authority of the Deputy Governor,SES, to

[1] The Basel Committee on Banking Supervision is a committee of banking supervisory authorities that was established by the central bank governors of the Group of Ten countries in 1975. It consists of senior representatives of bank supervisory authorities and central banks from Belgium, Canada, France, Germany, Italy, Japan, Luxembourg, the Netherlands, Spain, Sweden, Switzerland, the United Kingdom, and the United States. It usually meets at the Bank for International Settlements in Basel, Switzerland where its permanent Secretariat is located.

conduct on-site inspection outside of regular or special examination, for the purpose of ascertaining the accuracy of CAR calculations as well as the integrity of CAR monitoring and reporting systems.

Part II. Qualifying capital

1. Qualifying capital consists of Tier 1 (core plus hybrid) capital and Tier 2 (supplementary) capital elements, net of required deductions from capital.

A. Tier 1 Capital

2. Tier 1 capital is the sum of core Tier 1 capital and allowable amount of hybrid Tier 1 capital, as set in paragraph 12.

3. Core Tier 1 capital consists of:

a) Paid-up common stock;

b) Paid-up perpetual and non-cumulative preferred stock;

c) Additional paid-in capital;

d) Retained earnings;

e) Undivided profits (for domestic banks only);

f) Net gains on fair value adjustment of hedging instruments in a cash flow hedge of available for sale equity securities;

g) Cumulative foreign currency translation; and

h) Minority interest in subsidiary financial allied undertakings which are less than wholly-owned: *Provided*, That a bank shall not use minority interests in the equity accounts of consolidated subsidiaries as avenue for introducing into its capital structure elements that might not otherwise qualify as Tier 1 capital or that would, in effect, result in an excessive reliance on preferred stock within Tier 1:

Less:

i. Common stock treasury shares;

ii. Perpetual and non-cumulative preferred stock treasury shares;

iii. Net unrealized losses on available for sale equity securities purchased;

iv. Gains (Losses) resulting from designating financial liabilities at fair value through profit or loss that are due to own credit worthiness;

v. Unbooked valuation reserves and other capital adjustments based on the latest report of examination as approved by the Monetary Board;

vi. Total outstanding unsecured credit accommodations, both direct and indirect, to DOSRI and unsecured loans, other credit accommodations and guarantees granted to subsidiaries and affiliates;

vii. Deferred income tax;

viii. Goodwill, including that relating to unconsolidated subsidiary banks, financial allied undertakings, excluding subsidiary securities dealers/brokers and insurance companies, (on solo basis) and unconsolidated subsidiary securities dealers/brokers, insurance companies and non-financial allied undertakings (on solo and consolidated bases); and

ix. Gain on sale resulting from a securitization transaction.

4. Hybrid Tier 1 capital in the form of perpetual preferred stock and perpetual UnSD may be issued subject to prior BSP approval and to the conditions in paragraph 12.

5. In the case of foreign banks, Tier 1 capital is equivalent to:

a) Assigned capital including earnings not remitted to the head office which the bank elects to consider as part of assigned capital (in which case it can no longer be remitted to the head office); and

b) "Net due to" head office, branches, subsidiaries and other offices outside the Philippines as defined under Subsec. X105.5.d (inclusive of earnings not remitted to head office per Subsec. X105.5.c, unless considered as part of the assigned capital by the bank), subject to the limit prescribed under Subsec. X105.6,

Less:

i. Any balance in the "Net due from" account.

(As amended by Circular No. 560 dated 11 January 2007)

B. Tier 2 Capital

6. Tier 2 capital is the sum of UT2 capital and LT2 capital.

7. The total amount of LT2 capital before deductions enumerated in paragraph 10 that may be included in total Tier 2 capital shall be limited to a maximum of fifty percent (50%) of total Tier 1 capital (net of deductions enumerated in paragraph 3). The total amount of upper and lower Tier 2 capital both before deductions enumerated in paragraph 10 that may be included in total qualifying capital shall be limited to a maximum of 100% of total Tier 1 capital (net of deductions enumerated in paragraph 3).

8. UT2 capital consists of:

a) Paid-up perpetual and cumulative preferred stock;

b) Paid-up limited life redeemable preferred stock issued with the condition that redemption thereof shall be allowed only if the shares redeemed are replaced with at least an equivalent amount of newly paid-in shares so that the total paid-in capital stock is maintained at the same level prior to redemption;

c) Appraisal increment reserve – bank premises, as authorized by the Monetary Board;

d) Net unrealized gains on available for sale equity securities purchased subject to a fifty five percent (55%) discount;

e) General loan loss provision, limited to a maximum of one percent (1%) of credit risk-weighted assets, and any amount in excess thereof shall be deducted from the credit risk-weighted assets in computing the denominator of the risk-based capital ratio;

f) With prior BSP approval, UnSD with a minimum original maturity of at least ten (10) years issued subject to the conditions in paragraph 13, in an amount equivalent to its carrying amount discounted by the following rates:

Remaining maturity	Discount factor
5 years & above	0%
4 years to <5 years	20%
3 years to <4 years	40%
2 years to <3 years	60%
1 year to <2 years	80%
< 1 year	100%

g) Deposit for common stock subscription;

h) Deposit for perpetual and non-cumulative preferred stock subscription; and

i) Hybrid Tier 1 capital as defined in paragraph 4 in excess of the maximum allowable limit of fifteen percent (15%) of total Tier 1 capital (net of deductions enumerated in paragraph 3):

Less:

i. Perpetual and cumulative preferred stock treasury shares;

ii. Limited life redeemable preferred stock treasury shares with the replacement requirement upon redemption;

iii. Sinking fund for redemption of limited life redeemable preferred stock with the replacement requirement upon redemption; and

iv. Net losses in fair value adjustment of hedging instruments in a cash flow hedge of available for sale equity securities.

9. LT2 capital consists of:

a) Paid-up limited life redeemable preferred stock without the replacement requirement upon redemption in an amount equivalent to its carrying amount discounted by the following rates:

Remaining maturity	Discount factor
5 years & above	0%
4 years to <5 years	20%
3 years to <4 years	40%
2 years to <3 years	60%
1 year to <2 years	80%
< 1 year	100%

b) With prior BSP approval, UnSD with a minimum original maturity of at

least five (5) years, issued subject to the conditions in paragraph 14, in an amount equivalent to its carrying amount discounted by the following rates:

Remaining maturity	Discount factor
5 years & above	0%
4 years to <5 years	20%
3 years to <4 years	40%
2 years to <3 years	60%
1 year to <2 years	80%
< 1 year	100%

c) Deposit for perpetual and cumulative preferred stock subscription; and

d) Deposit for limited life redeemable preferred stock subscription with the replacement requirement upon redemption.

Less:

i. Limited life redeemable preferred stock treasury shares without the replacement requirement upon redemption; and

ii. Sinking fund for redemption of limited life redeemable preferred stock without the replacement requirement upon redemption up to the extent of the balance of redeemable preferred stock after applying the cumulative discount factor.

C. Deductions from the total of Tier 1 and Tier 2 capital

10. The following items should be deducted fifty percent (50%) from Tier 1 and fifty percent (50%) from Tier 2 capital:

a) Investments in equity of unconsolidated subsidiary banks and QBs, and other financial allied undertakings (excluding subsidiary securities dealers/ brokers and insurance companies), after deducting related goodwill, if any (for solo basis);

b) Investments in other regulatory capital instruments of unconsolidated subsidiary banks and QBs (for solo basis);

c) Investments in equity of unconsolidated subsidiary securities dealers/brokers, insurance companies, and non-financial allied undertakings, after deducting related goodwill, if any (for both solo and consolidated bases);

d) Capital shortfalls of unconsolidated subsidiary securities dealers/brokers and insurance companies (for both solo and consolidated bases);

e) Significant minority investments (20%-50% of voting stock) in banks and QBs, and other financial allied undertakings (for both solo and consolidated bases);

f) Reciprocal investments in equity of other banks/enterprises;

g) Reciprocal investments in other regulatory capital instruments of other banks and QBs;

h) Materiality thresholds in credit derivative contracts purchased;

i) Securitization tranches which are rated below investment grade or are unrated; and

j) Credit enhancing interest only strips in relation to a securitization structure, net of the amount of "gain-on-sale" that must be deducted from core Tier 1 capital referred to in paragraph 3.

11. Any asset deducted from qualifying capital in computing the numerator of the risk-based capital ratio shall not be included in the risk-weighted assets in computing the denominator of the ratio. Available for sale debt securities shall be risk-weighted net of specific provisions as provided in paragraph 1 of Part III.A, but without considering accumulated market gains/ losses.

D. Eligible instruments under hybrid Tier 1 capital

12. Perpetual preferred stock and perpetual UnSD issuances of banks should comply with the following minimum conditions in order to be eligible as hybrid Tier 1 (HT1) capital:

a) It must be issued and fully paid-up. Only the net proceeds received from the issuance shall be included as capital;

b) The dividends/coupons must be non-cumulative. It is acceptable to pay dividends/coupons in scrip or shares of stock if a cash dividend/coupon is withheld: *Provided,* That this does not result on issuing lower quality capital: *Provided, further,* That where such dividend/coupon stock settlement feature is included, the bank should ensure that it has an appropriate buffer of authorized capital stock and appropriate stockholders and board authorization, if necessary, to fulfill their potential obligations under such issues;

c) It must be available to absorb losses of the bank without it being obliged to cease carrying on business. The agreement governing its issuance should specifically provide for the dividend/ coupon and principal to absorb losses where the bank would otherwise be insolvent, or for its holders to be treated as if they were holders of a specified class of share capital in any proceedings commenced for the winding up of the bank. Issue documentation must disclose to prospective investors the manner by which the instrument is to be treated in loss situation.

Alternatively, the agreement governing its issuance can provide for automatic conversion into common shares or perpetual and non-cumulative preferred shares upon occurrence of certain trigger events, as follows:

i. Breach of minimum capital ratio;

ii. Commencement of proceedings for winding up of the bank; or

iii. Upon appointment of receiver for the bank.

The rate of conversion must be fixed at the time of subscription to the instrument. The bank must also ensure that it has appropriate buffer of authorized capital stock and appropriate stockholders and board authorization for conversion/ issue to take place anytime;

d) Its holders must not have a priority claim, in respect of principal and dividend/ coupon payments in the event of winding up of the bank, which is higher than or equal with that of depositors, other creditors of the bank and holders of LT2 and UT2 capital instruments. Its holder must waive his right to set-off any amount he owes the bank against any subordinated amount owed to him due to the HT1 capital instrument;

e) It must neither be secured nor covered by a guarantee of the issuer or related party or other arrangement that legally or economically enhances the priority of the claim of any holder as against depositors, other creditors of the bank and holders of LT2 and UT2 capital instruments;

f) It must not be redeemable at the initiative of the holder. It must not be repayable without the prior approval of the BSP: *Provided*, That repayment may be allowed only in connection with call option after a minimum of five (5) years from issue date: *Provided, however*, That a call option may be exercised within the first five (5) years from issue date when –

i. It was issued for the purpose of a merger with or acquisition by the bank and the merger or acquisition is aborted;

ii. There is a change in tax status of the HT1 capital instrument due to changes in the tax laws and/or regulations; or

iii. It does not qualify as HT1 capital as determined by the BSP:

Provided, further, That such repayment shall be approved by the BSP only if the preferred share/debt is simultaneously replaced with issues of new capital which is neither smaller in size nor of lower quality than the original issue, unless the bank's capital ratio remains more than adequate after redemption.

It must not contain any clause which requires acceleration of payment of

principal, except in the event of insolvency. The agreement governing its issuance must not contain any provision that mandates or creates an incentive for the bank to repay the outstanding principal of the instrument, e.g., a cross-default or negative pledge or a restrictive covenant, other than a call option which may be exercised by the bank;

g) Its main features must be publicly disclosed by annotating the same on the instrument and in a manner that is easily understood by the investor;

h) The proceeds of the issuance must be immediately available without limitation to the bank;

i) The bank must have full discretion over the amount and timing of dividends/ coupons where the bank –

i. Has not paid or declared a dividend on its common shares in the preceding financial year; or

ii. Determines that no dividend is to be paid on such shares in the current financial year.

The bank must have full control and access to waived payments;

j) Any dividend/coupon to be paid must be paid only to the extent that the bank has profits distributable determined in accordance with existing BSP regulations. The dividend/coupon rate, or the formulation for calculating dividend/ coupon payments must be fixed at the time of issuance and must not be linked to the credit standing of the bank;

k) It may allow only one (1) moderate step-up in the dividend/coupon rate in conjunction with a call option, only if the step-up occurs at a minimum of ten (10) years after the issue date and if it results in an increase over the initial rate that is not more than:

i. 100 basis points less the swap spread between the initial index basis and the stepped-up index basis; or

ii. fifty percent (50%) of the initial credit spread less the swap spread between the initial index basis and the stepped-up index basis.

The swap spread should be fixed as of the pricing date and reflect the differential in pricing on that date between the initial reference security or rate and the stepped-up reference security or rate.

l) It must be underwritten by a third party not related to the issuer bank nor acting in reciprocity for and in behalf of the issuer bank;

m) It must be issued in minimum denominations of at least ₱500,000.00 or its equivalent;

n) It must clearly state on its face that it is not a deposit and is not insured by the PDIC; and

o) The bank must submit a written external legal opinion that the abovementioned requirements, including the subordination and loss absorption features, have been met:

Provided, That for purposes of reserve requirement regulation, it shall not be treated as time deposit liability, deposit substitute liability or other forms of borrowings: *Provided, further,* That the total amount of HT1 capital that may be included in the Tier 1 capital shall be limited to a maximum of fifteen percent (15%) of total Tier 1 capital (net of deductions enumerated in paragraph 3): *Provided, furthermore,* That the amount of HT1 capital in excess of the maximum limit shall be eligible for inclusion in the UT2 capital, subject to the limit in total Tier 2 capital. To determine the allowable amount of HT1 capital, the amount of total core Tier 1 capital (net of deductions enumerated in paragraph 3) should be multiplied by seventeen and sixty five percent (17.65%), the number derived from the proportion of fifteen percent (15%) to eighty five percent (85%), i.e., 15%/85% = 17.65%.

E. Eligible unsecured subordinated debt

13. UnSD issuances by banks should comply with the following minimum

conditions in order to be eligible as UT2 capital:

a) It must be issued and fully paid-up. Only the net proceeds received from the issuance shall be included as capital;

b) It must be available to absorb losses of the bank without it being obliged to cease carrying on business. The agreement governing its issuance should specifically provide for the coupon and principal to absorb losses where the bank would otherwise be insolvent, or for its holders to be treated as if they were holders of a specified class of share capital in any proceedings commenced for the winding up of the bank. Issue documentation must disclose to prospective investors the manner by which the instrument is to be treated in loss situation.

Alternatively, the agreement governing its issuance can provide for automatic conversion into common shares or perpetual and non-cumulative shares or perpetual and cumulative preferred shares upon occurrence of certain trigger events, as follows:

i. Breach of minimum capital ratio;

ii. Commencement of proceedings for winding up of the bank; or

iii. Upon appointment of receiver for the bank.

The rate of conversion must be fixed at the time of subscription to the instrument. The bank must also ensure that it has appropriate buffer of authorized capital stock and appropriate stockholders and board authorization for conversion/ issue to take place anytime;

c) Its holders must not have priority claim, in respect of principal and coupon payments in the event of winding up of the bank, which is higher than or equal with that of depositors, other creditors of the bank, and holders of LT2 capital instruments. Its holder must waive his right to set off any amount he owes the bank against any subordinated amount owed to him due to the UT2 capital instrument;

d) It must neither be secured nor covered by a guarantee of the issuer or related party or other arrangement that legally or economically enhances the priority of the claim of any holder as against depositors, other creditors of the bank and holders of LT2 capital instruments;

e) It must not be redeemable at the initiative of the holder. It must not be repayable prior to maturity without the prior approval of the BSP: *Provided*, That repayment may be allowed only in connection with a call option after a minimum of five (5) years from issue date: *Provided, however*, That a call option may be exercised within the first five (5) years from issue date when:

i. It was issued for the purpose of a merger with or acquisition by the bank and the merger or acquisition is aborted;

ii. There is a change in tax status of the UT2 capital instrument due to changes in the tax laws and/or regulations; or

iii. It does not qualify as UT2 capital as determined by the BSP:

Provided, further, That such repayment prior to maturity shall be approved by the BSP only if the debt is simultaneously replaced with issues of new capital which is neither smaller in size nor of lower quality than the original issue, unless the bank's capital ratio remains more than adequate after redemption.

It must not contain any clause which requires acceleration of payment of principal, except in the event of insolvency. The agreement governing its issuance must not contain any provision that mandates or creates an incentive for the bank to repay the outstanding principal of the instrument, e.g., a cross-default or negative pledge or a restrictive covenant, other than a call option which may be exercised by the bank;

f) Its main features must be publicly disclosed by annotating the same on the

instrument and in a manner that is easily understood by the investor;

g) The proceeds of the issuance must be immediately available without limitation to the bank;

h) The bank must have the option to defer any coupon payment where the bank:

i. has not paid or declared a dividend on its common shares in the preceding financial year; or

ii. determines that no dividend is to be paid on such shares in the current financial year;

It is acceptable for the deferred coupon to bear interest but the interest rate payable must not exceed market rates;

i) The coupon rate, or the formulation for calculating coupon payments must be fixed at the time of issuance and must not be linked to the credit standing of the bank;

j) It may allow only one (1) moderate step-up in the coupon rate in conjunction with a call option, only if the step-up occurs at a minimum of ten (10) years after the issue date and if it results in an increase over the initial rate that is not more than:

i. 100 basis points less the swap spread between the initial index basis and the stepped-up index basis; or

ii. fifty percent (50%) of the initial credit spread less the swap spread between the initial index basis and the stepped-up index basis.

The swap spread should be fixed as of the pricing date and reflect the differential in pricing on that date between the initial reference security or rate and the stepped-up reference security or rate;

k) It must be underwritten by a third party not related to the issuer bank nor acting in reciprocity for and in behalf of the issuer bank;

l) It must be issued in minimum denominations of at least ₱500,000.00 or its equivalent;

m) It must clearly state on its face that it is not a deposit and is not insured by the PDIC; and

n) The bank must submit a written external legal opinion that the abovementioned requirements, including the subordination and loss absorption features, have been met:

Provided, That it shall be subject to a cumulative discount factor of twenty percent (20%) per year during the last five (5) years to maturity [i.e., twenty percent (20%) if the remaining life is four (4) years to less than five (5) years, forty percent (40%) if the remaining life is three (3) years to less than four (4) years, etc.]: *Provided, further,* That where it is denominated in a foreign currency, it shall be revalued in accordance with PAS 21: *Provided, furthermore,* That for purposes of reserve requirement regulation, it shall not be treated as time deposit liability, deposit substitute liability or other forms of borrowings.

14. UnSD issuances by banks should comply with the following minimum conditions in order to be eligible as LT2 capital:

a) It must be issued and fully paid-up. Only the net proceeds received from the issuance shall be included as capital;

b) Its holders must not have priority claim, in respect of principal and coupon payments in the event of winding up of the bank, which is higher than or equal with that of depositors and other creditors of the bank. Its holder must waive his right to set-off any amount he owes the bank against any subordinated amount owed to him due to the LT2 capital instrument;

c) It must neither be secured nor covered by a guarantee of the issuer or related party or other arrangement that legally or economically enhances the priority of the claim of any holder as against depositors and other creditors of the bank;

d) It must not be redeemable at the initiative of the holder. It must not be

repayable prior to maturity without the prior approval of the BSP:

Provided, That repayment may be allowed only in connection with a call option after a minimum of five (5) years from issue date: *Provided, however*, That a call option may be exercised within the first five (5) years from issue date when:

i. It was issued for the purpose of a merger with or acquisition by the bank and the merger or acquisition is aborted;

ii. There is a change in tax status of the LT2 capital instrument due to changes in the tax laws and/or regulations; or

iii. It does not qualify as LT2 capital as determined by the BSP:

Provided, further, That such repayment prior to maturity shall be approved by the BSP only if the debt is simultaneously replaced with issues of new capital which is neither smaller in size nor of lower quality than the original issue, unless the bank's capital ratio remains more than adequate after redemption.

It must not contain any clause which requires acceleration of payment of principal, except in the event of insolvency. The agreement governing its issuance must not contain any provision that mandates or creates an incentive for the bank to repay the outstanding principal of the instrument, e.g., a cross-default or negative pledge or a restrictive covenant, other than a call option which may be exercised by the bank;

e) Its main features must be publicly disclosed by annotating the same on the instrument and in a manner that is easily understood by the investor;

f) The proceeds of the issuance must be immediately available without limitation to the bank;

g) The coupon rate, or the formulation for calculating coupon payments must be fixed at the time of issuance and must not be linked to the credit standing of the bank;

h) It may allow only one (1) moderate step-up in the coupon rate in conjunction with a call option, only if the step-up occurs at a minimum of five (5) years after the issue date and if it results in an increase over the initial rate that is not more than:

i. 100 basis points less the swap spread between the initial index basis and the stepped-up index basis; or

ii. fifty percent (50%) of the initial credit spread less the swap spread between the initial index basis and the stepped-up index basis.

The swap spread should be fixed as of the pricing date and reflect the differential in pricing on that date between the initial reference security or rate and the stepped-up reference security or rate;

i) It must be underwritten by a third party not related to the issuer bank nor acting in reciprocity for and in behalf of the issuer bank;

j) It must be issued in minimum denominations of at least ₱500,000.00 or its equivalent;

k) It must clearly state on its face that it is not a deposit and is not insured by the PDIC; and

l) The bank must submit a written external legal opinion that the abovementioned requirements, including the subordination features, have been met:

Provided, That it shall be subject to a cumulative discount factor of twenty percent (20%) per year during the last five (5) years to maturity [i.e., twenty percent (20%) if the remaining life is four (4) years to less than five (5) years, forty percent (40%) if the remaining life is three (3) years to less than four (4) years, etc.]: *Provided, further,* That where it is denominated in a foreign currency, it shall be revalued in accordance with PAS 21: *Provided, furthermore,* That for purposes of reserve requirement regulation, it shall not be treated as time deposit liability, deposit substitute liability or other forms of borrowings.

Part III. Credit risk-weighted assets

A. Risk-weighting

1. Banking book exposures shall be risk-weighted based on third party credit assessment of the individual exposure given by eligible external credit assessment institutions listed in Part III.C. The table below sets out the mapping of external credit assessments with the corresponding risk weights for banking book exposures. Exposures related to credit derivatives and securitizations are dealt with in Parts IV and V, respectively. Exposures should be risk-weighted net of specific provisions.

STANDARDIZED CREDIT RISK WEIGHTS								
Credit Assessment[1]	AAA	AA+ to AA-	A+ to A-	BBB+ to BBB-	BB+ to BB-	B+ to B-	Below B-	Unrated
Sovereigns	0%	0%	20%	50%	100%	100%	150%	100%
MDBs	0%	20%	50%	50%	100%	100%	150%	100%
Banks	20%	20%	50%	50%	100%	100%	150%	100%[2]
Interbank call loans	20%							
Local government units	20%	20%	50%	50%	100%	100%	150%	100%[2]
Government corporations	20%	20%	50%	100%	100%	150%	150%	100%[2]
Corporates	20%	20%	50%	100%	100%	150%	150%	100%[2]
Housing loans	50%							
MSME qualified portfolio	75%							
Defaulted exposures								
Housing loans	100%							
Others	150%							
ROPA	150%							
All other assets	100%							

Sovereign Exposures

2. These include all exposures to central governments and central banks. All Philippine peso (Php) denominated exposures to the Philippine National Government (NG) and the BSP shall be risk-weighted at zero percent (0%). Foreign currency denominated exposures to the NG and the BSP, however, shall be risk-weighted according to the table above: *Provided,* That only one-third (1/3) of the applicable risk weight shall be applied from 01 July 2007, two-thirds (2/3) from 01 January 2008, and the full risk weight from 01 January 2009[3]. Exposures to the Bank for International Settlements (BIS), the International Monetary Fund (IMF), and the European Central Bank (ECB) and the European Community (EC) shall also receive zero percent (0%) risk weight.

(As amended by Circular No. 588 dated 11 December 2007)

MDB Exposures

3. These include all exposures to multilateral development banks. Exposures to the World Bank Group comprised of the IBRD and the IFC, the ADB, the AfDB, the EBRD, the IADB, the EIB, the European Investment Fund (EIF), the NIB, the CDB, the Islamic Development Bank (IDB), and the CEDB currently receive zero percent (0%) risk weight. However, it is the responsibility of the bank to monitor the external credit assessments of multilateral development banks to which they have an exposure to reflect in the risk weights any change therein.

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[1] The notations follow the rating symbols used by Standard & Poor's. The mapping of ratings of all recognized external rating agencies is in Part III.C

[2] Or risk weight applicable to sovereign of incorporation, whichever is higher

[3] The capital treatment of QB's holdings of ROP Global Bonds paired with Warrants under the BSP's revised risk-based capital adequacy framework is contained in *Appendix Q-46a*.

Bank Exposures

4. These include all exposures to Philippine-incorporated banks/QBs, as well as foreign-incorporated banks.

Interbank Call Loans

5. Interbank call loans refer to interbank loans that pass through the Interbank Call Loan Funds Transfer System of the BSP, the BAP, and the PCHC.

Exposures to Local Government Units

6. These include all exposures to non-central government public sector entities. Bonds issued by Philippine local government units (LGU Bonds), which are covered by Deed of Assignment of Internal Revenue Allotment of the LGU and guaranteed by the LGU Guarantee Corporation shall be risk-weighted at the lower of fifty percent (50%) or the appropriate risk weight indicated in the table above.

Exposures to Government Corporations

7. These include all exposures to commercial undertakings owned by central or local governments. Exposures to Philippine GOCCs that are not explicitly guaranteed by the Philippine NG are also included in this category.

Corporate Exposures

8. These include all exposures to business entities, which are not considered as micro, small, or medium enterprises (MSME), whether in the form of a corporation, partnership, or sole-proprietorship. These also include all exposures to FIs, including securities dealers/ brokers and insurance companies, not falling under the definition of *Bank* in paragraph 4.

Housing Loans

9. These include all current loans to individuals for housing purpose, fully secured by first mortgage on residential property that is or will be occupied by the borrower.

Micro, Small, and Medium Enterprises

10. An exposure must meet the following criteria to be considered as an MSME exposure:

a) The exposure must be to an MSME as defined under existing BSP regulations; and

b) The exposure must be in the form of direct loans, or unavailed portion of committed credit lines and other business facilities such as outstanding guarantees issued and unused letters of credit: *Provided*, That the credit equivalent amounts thereof shall be determined in accordance with the methodology for off-balance sheet items.

Qualified portfolio

11. For a bank's portfolio of MSME exposures to be considered as *qualified*, it must be a highly diversified portfolio, i.e., it has at least 500 borrowers that are distributed over a number of industries. In addition, all MSME exposures in the qualified portfolio must be current exposures. All non-current MSME exposures are excluded from count and are to be treated as ordinary non-performing loans. Current MSME exposures not qualifying under highly diversified MSME portfolio will be risk-weighted based on external rating and shall be risk-weighted in the same manner as corporate exposures.

Defaulted Exposures

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

a) If a credit obligation is considered non-performing under existing rules and regulations. For non-performing debt securities, they shall be defined as follows:

i. For zero-coupon debt securities, and debt securities with quarterly, semi-annual, or annual coupon payments, they shall be considered non-performing when principal and/or coupon payment,

as may be applicable, is unpaid for thirty (30) days or more after due date; and

ii. For debt securities with monthly coupon payments, they shall be considered non-performing when three (3) or more coupon payments are in arrears: *Provided, however*, That when the total amount of arrearages reaches twenty percent (20%) of the total outstanding balance of the debt security, the total outstanding balance of the debt security shall be considered as non-performing.

b) 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;

c) 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 must specifically define when a material credit-related loss occurs; and

d) 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.

Housing loans

13. These include all loans to individuals for housing purpose, fully secured by first mortgage on residential property that is or will be occupied by the borrower, which are considered to be in default in accordance with paragraph 12.

Others

14. These include the total amounts or portions of all other defaulted exposures, which are not secured by eligible collateral or guarantee as defined in Part III.B.

ROPA

15. All real and other properties acquired and classified as such under existing regulations.

Other Assets

16. The standard risk weight for all other assets, including bank premises, furniture, fixtures and equipment, will be 100%, except in the following cases:

a) Cash on hand and gold, which shall be risk-weighted at zero percent (0%); and

b) Checks and other cash items, which shall be risk-weighted at twenty percent (20%).

Accruals on a claim shall be classified and risk-weighted in the same way as the claim. Bills purchased shall be classified and risk-weighted as claims on the drawee bank. The treatments of credit derivatives and securitization exposures are presented separately in Parts IV and V, respectively. Investments in equity or other regulatory capital instruments issued by banks or other financial/non-financial allied/non-allied undertakings will be risk-weighted at 100%, unless deductible from the capital base as required in Part II.

Off-balance sheet items

17. For off-balance sheet items, the risk-weighted amount shall be calculated using a two-step process. First, the credit equivalent amount of an off-balance sheet item shall be determined by multiplying its notional principal amount by the appropriate credit conversion factor, as follows:

a) *100% credit conversion factor* - this shall apply to direct credit substitutes, e.g., general guarantees of indebtedness (including standby letters of credit serving as financial guarantees for loans and securities) and acceptances (including endorsements with the character of acceptances), and shall include:

i. Guarantees issued other than shipside bonds/airway bills;

ii. Financial standby letters of credit

b) *Fifty percent (50%) credit conversion factor* – this shall apply to certain transaction-related contingent items, e.g., performance bonds, bid bonds,

warranties and standby letters of credit related to particular transactions, and shall include:

i. Performance standby letters of credit (net of margin deposit), established as a guarantee that a business transaction will be performed;

This shall also apply to –

i. Note issuance facilities and revolving underwriting facilities; and

ii. Other commitments, e.g., formal standby facilities and credit lines with an original maturity of more than one (1) year, and this shall also include Underwritten Accounts Unsold.

c) *Twenty percent (20%) credit conversion factor* – this shall apply to short-term, self-liquidating trade-related contingencies arising from movement of goods, e.g., documentary credits collateralized by the underlying shipments, and shall include:

i. Trade-related guarantees:
   - Shipside bonds/airway bills
   - Letters of credit – confirmed

ii. Sight letters of credit outstanding (net of margin deposit);

iii. Usance letters of credit outstanding (net of margin deposit);

iv. Deferred letters of credit (net of margin deposit); and

v. Revolving letters of credit (net of margin deposit) arising from movement of goods and/or services;

This shall also apply to commitments with an original maturity of up to one (1) year, and shall include Committed Credit Line for Commercial Paper Issued.

d) *Zero percent (0%) credit conversion factor* – this shall apply to commitments which can be unconditionally cancelled at any time by the bank without prior notice, and shall include Credit Card Lines.

This shall also apply to those not involving credit risk, and shall include:

i. Late deposits/payments received;
ii. Inward bills for collection;
iii. Outward bills for collection;
iv. Travelers' checks unsold;
v. Trust department accounts;
vi. Items held for safekeeping/ custodianship;
vii. Items held as collaterals;
viii. Deficiency claims receivable; and
ix. Others.

18. For derivative contracts, the credit equivalent amount shall be the sum of the current credit exposure (or replacement cost) and an estimate of the potential future credit exposure (or add-on). However, the following shall not be included in the computation:

a) Instruments which are traded in an exchange where they are subject to daily receipt and payment of cash variation margin; and

b) Exchange rate contract with original maturity of fourteen (14) calendar days or less.

19. The current credit exposure shall be the positive mark-to-market value of the contract (or zero if the mark-to-market value is zero or negative). The potential future credit exposure shall be the product of the notional principal amount of the contract multiplied by the appropriate potential future credit conversion factor, as indicated below:

Residual Maturity	Interest Rate Contract	Exchange Rate Contract	Equity Contract
One (1) year or less	0.0%	1.0%	6.0%
Over one (1) year to five (5) years	0.5%	5.0%	8.0%
Over five (5) years	1.5%	7.5%	10.0%

Provided, That:

a) For contracts with multiple exchanges of principal, the factors are to be multiplied by the number of remaining payments in the contract;

b) For contracts that are structured to settle outstanding exposure following specified payment dates and where the terms are reset such that the market value of the contract is zero on these specified dates, the residual maturity would be set

equal to the time until the next reset date, and in the case of interest rate contracts with remaining maturities of more than one (1) year that meet these criteria, the potential future credit conversion factor is subject to a floor of one-half percent (1/2%); and

c) No potential future credit exposure shall be calculated for single currency floating/floating interest rate swaps, i.e., the credit exposure on these contracts would be evaluated solely on the basis of their mark-to-market value.

20. The credit equivalent amount shall be treated like any on-balance sheet asset, and shall be assigned the appropriate risk weight, i.e., according to the third party credit assessment of the counterparty exposure.

B. Credit risk mitigation (CRM)

21. Banks use a number of techniques to mitigate the credit risks to which they are exposed. For example, exposures may be collateralized by first priority claims, in whole or in part with cash or securities, or a loan exposure may be guaranteed by a third party. Physical collateral, such as real estate, buildings, machineries, and inventories are not recognized at this time for credit risk mitigation purposes in line with Basel II recommendations.

22. In order for banks to obtain capital relief for any use of CRM techniques, all documentation used in collateralized transactions and for documenting guarantees must be binding on all parties and legally enforceable in all relevant jurisdictions. Banks must have conducted sufficient legal review to verify this and have a well-founded legal basis to reach this conclusion, and undertake such further review as necessary to ensure continuing enforceability.

23. The effects of CRM will not be double counted. Therefore, no additional supervisory recognition of CRM for regulatory capital purposes will be granted on claims for which an issue-specific rating is used that already reflects that CRM. Principal-only ratings will not be allowed within the framework of CRM.

24. While the use of CRM techniques reduces or transfers credit risk, it simultaneously may increase other risks (residual risks). Residual risks include legal, operational, liquidity and market risks. Therefore, it is imperative that banks employ robust procedures and processes to control these risks, including strategy; consideration of the underlying credit; valuation; policies and procedures; systems; control of roll-off risks; and management of concentration risk arising from the bank's use of CRM techniques and its interaction with the bank's overall credit risk profile.

25. The disclosure requirements under Part VIII of this document must also be observed for banks to obtain capital relief (i.e., adjustments in the risk weights of collateralized or guaranteed exposures) in respect of any CRM techniques.

Collateralized transactions

26. A collateralized transaction is one in which:

a) banks have a credit exposure or potential credit exposure; and

b) that credit exposure or potential credit exposure is hedged in whole or in part by collateral posted by a counterparty[1] or by a third party in behalf of the counterparty.

27. In addition to the general requirement for legal certainty set out in paragraph 22, the legal mechanism by which collateral is pledged or transferred must ensure that the bank has the right to liquidate or take legal possession of it, in a timely manner, in the event of default, insolvency or bankruptcy (or one or more otherwise-defined credit events set out in the transaction documentation) of the counterparty (and, where applicable, of the

[1] *Counterparty* refers to a party to whom a bank has an on- or off-balance sheet credit exposure or a potential credit exposure.

custodian holding the collateral). Furthermore, banks must take all steps necessary to fulfill those requirements under the law applicable to the bank's interest in the collateral for obtaining and maintaining an enforceable security interest, e.g., by registering it with a registrar, or for exercising a right to net or set off in relation to title transfer collateral.

28. In order for collateral to provide protection, the credit quality of the counterparty and the value of the collateral must not have a material positive correlation. For example, securities issued by the counterparty – or by any related group entity – would provide little protection and so would be ineligible.

29. Banks must have clear and robust procedures for the timely liquidation of collateral to ensure that any legal conditions required for declaring the default of the counterparty and liquidating the collateral are observed, and that collateral can be liquidated promptly.

30. Where the collateral is required to be held by a custodian, the BSP will only recognize the collateral for regulatory capital purposes if it is held by BSP-authorized third party custodians.

31. A capital requirement will be applied to a bank on either side of the collateralized transaction: for example, both repos and reverse repos will be subject to capital requirements. Likewise, both sides of a securities lending and borrowing transaction will be subject to explicit capital charges, as will the posting of securities in connection with a derivative exposure or other borrowing.

Banking book

32. Where banks take eligible collateral, as listed in paragraph 34, and satisfies the requirements under paragraphs 27 to 31, they are allowed to apply the risk weight of the collateral to the collateralized portion of the credit exposure (equivalent to the fair market value of recognized collateral), subject to a floor of twenty percent (20%). The twenty percent (20%) floor shall not apply and a zero percent (0%) risk weight can be applied when the exposure and the collateral are denominated in the same currency, and either:

a) The collateral is cash as defined in paragraph 34.a; or

b) The collateral is a sovereign debt security eligible for zero percent (0%) risk weight, or a Php-denominated debt obligation issued by the Philippine NG or the BSP, which fair market value has been discounted by twenty percent (20%).

33. For collateral to be recognized, however, the collateral must be pledged for at least the life of the exposure and it must be marked to market and revalued with a minimum frequency of every six (6) months.

34. The following are the eligible collateral instruments:

a) Cash (as well as certificates of deposit or comparable instruments issued by the lending bank) on deposit with the bank which is incurring the counterparty exposure;

b) Gold;

c) Debt obligations issued by the Philippine NG or the BSP;

d) Debt securities issued by central governments and central banks (and PSEs treated as sovereigns) of foreign countries as well as MDBs with at least investment grade external credit ratings;

e) Other debt securities with external credit ratings of at least BBB- or its equivalent;

f) Unrated senior debt securities issued by banks with an issuer rating of at least BBB- or its equivalent, or with other debt issues of the same seniority with a rating of at least BBB- or its equivalent;

g) Equities included in the main index of an organized exchange; and

h) Investments in Unit Investment Trust Funds (UITF) and the Asian Bond Fund 2 (ABF2) duly approved by the BSP.

Trading book

35. A credit risk capital requirement should also be applied to banks' counterparty exposures in the trading book (e.g., repo-style transactions, OTC derivatives contracts). Where banks take eligible collateral for these trading book transactions, as listed in paragraph 34, and satisfies the requirements under paragraphs 27 to 31, they are to compute for the credit risk capital requirement according to the following paragraphs: *Provided,* That, for repo-style transactions in the trading book, all instruments which are included in the trading book may be used as eligible collateral.

36. For collateralized transactions in the trading book, the exposure amount after risk mitigation is calculated as follows:

$E^* = \max \{0, [E \times (1 + H_e) - C \times (1 - H_c - H_{fx})]\}$

Where:

E^* = the exposure value after risk mitigation
E = the current value of the exposure
H_e = haircut appropriate to the exposure
C = the current value of the collateral received
H_c = haircut appropriate to the collateral
H_{fx} = haircut appropriate for currency mismatch between the collateral and exposure set at 8% (based on a 10-business day holding period and daily marking to market)

37. The treatment of transactions where there is a maturity mismatch between the maturity of the counterparty exposure and the collateral is given in paragraphs 50 to 54.

38. These are the haircuts to be used (based on a 10-business day holding period, daily marking to market and daily remargining), expressed as percentages:

Issue rating for debt securities[1]	Residual maturity	Haircut	
		Sovereign (and PSEs treated as sovereign) and MDB (with 0% risk weight) issuers	Other Issuers
Php – denominated securities issued by the Philippine NG and BSP	≤ 1 year	0.5	
	> 1 yr. to ≤ 5 yrs.	2	
	> 5 years	4	
AAA to AA-	≤ 1 year	0.5	1
	> 1 yr. to ≤ 5 yrs.	2	4
	> 5 years	4	8
A+ to BBB-/ Unrated bank debt securities as defined in paragraph 34.f	≤ 1 year	1	2
	> 1 yr. to ≤ 5 yrs	3	6
	> 5 years	6	12
Equities included in the main index and gold		15	
UITF and ABF2		Highest haircut applicable to any security in which the fund can invest	
Cash per paragraph 34.a in the same currency		0	
Other financial instruments in the trading book (applies to repo-style transactions in the trading book only)		25	

39. Where the collateral is a basket of assets, the haircut on the basket will be $H = \Sigma a_i H_i$, where a_i is the weight of the asset in the basket and H_i is the haircut applicable to that asset.

40. For collateralized OTC derivatives transactions in the trading book, the credit equivalent amount will be computed according to paragraphs 18 to 19, but adjusted by deducting the volatility adjusted collateral amount as computed according to paragraphs 36 to 39.

[1] The notations follow the rating symbols used by Standard & Poor's. The mapping of ratings of all recognized external rating agencies is in Part III.C

41. The exposure amount after risk mitigation will be multiplied by the risk weight of the counterparty to obtain the risk-weighted asset amount for the collateralized transaction.

Guarantees

42. Where guarantees are direct, explicit, irrevocable and unconditional, banks may be allowed to take account of such credit protection in calculating capital requirements.

43. A guarantee must represent a direct claim on the protection provider and must be explicitly referenced to specific exposures or a pool of exposures, so that the extent of the cover is clearly defined and incontrovertible. Other than non-payment by a protection purchaser of money due in respect of the credit protection contract, the guarantee must be irrevocable; there must be no clause in the contract that would allow the protection provider unilaterally to cancel the credit cover or that would increase the effective cost of cover as a result of deteriorating credit quality in the hedged exposure. It must also be unconditional; there should be no clause in the protection contract outside the direct control of the bank that could prevent the protection provider from being obliged to pay out in a timely manner in the event that the original counterparty fails to make the payment(s) due.

44. In addition to the legal certainty requirement in paragraph 22, in order for a guarantee to be recognized, the following conditions must be satisfied:

a) On the qualifying default/ non-payment of the counterparty, the bank may in a timely manner pursue the guarantor for any monies outstanding under the documentation governing the transaction. The guarantor may make one lump sum payment of all monies under such documentation to the bank, or the guarantor may assume the future payment obligations of the counterparty covered by the guarantee. The bank must have the right to receive any such payments from the guarantor without first having to take legal actions in order to pursue the counterparty for payment;

b) The guarantee is an explicitly documented obligation assumed by the guarantor; and

c) The guarantee must cover all types of payments the underlying obligor is expected to make under the documentation governing the transaction, for example, notional amount, margin payments, etc. Where a guarantee covers payment of principal only, interests and other uncovered payments should be treated as an unsecured amount.

45. Where the bank's exposure is guaranteed by an eligible guarantor, as listed in paragraph 47, and satisfies the requirements under paragraphs 42 to 44, the bank is allowed to apply the risk weight of the guarantor to the guaranteed portion of the credit exposure.

46. The treatment of transactions where there is a mismatch between the maturity of the counterparty exposure and the guarantee is given in paragraphs 50 to 54.

47. The following are the eligible guarantors:

a) Philippine NG and the BSP;

b) Central governments and central banks and PSEs of foreign countries as well as MDBs with a lower risk weight than the counterparty;

c) Banks with a lower risk weight than the counterparty; and

d) Other entities with external credit assessment of at least A- or its equivalent.

48. Where a bank provides a credit protection to another bank in the form of a guarantee that a third party will perform on its obligations, the risk to the guarantor bank is the same as if the bank had entered into the transaction as a principal. In such circumstances, the guarantor bank will be required to calculate capital requirement on the guaranteed amount according to the

risk weight corresponding to the third party exposure. In this instance, and provided the credit protection is deemed to be legally effective, the credit risk is considered transferred to the bank providing credit protection. However, the bank receiving credit protection on its exposure to a third party shall recognize a corresponding risk-weighted credit exposure to the bank providing credit protection.

49. An exposure that is covered by a guarantee that is counter-guaranteed by the Philippine NG or BSP, may be considered as covered by the guarantee of the Philippine NG or BSP: *Provided,* That:

a) the counter-guarantee covers all credit risk element of the exposure;

b) both the original guarantee and the counter-guarantee meet all operational requirements for guarantees, except that the counter guarantee need not be direct and explicit to the original exposure; and

c) the cover is robust and that no historical evidence suggests that the coverage of the counter-guarantee is less than effectively equivalent to that of a direct guarantee of the Philippine NG and BSP.

Currently, Php-denominated exposures to the extent guaranteed by Industrial Guarantee and Loan Fund (IGLF), Home Guaranty Corporation (HGC), and Trade and Investment Development Corporation of the Philippines (TIDCORP), which guarantees are counter-guaranteed by the Philippine NG receive zero percent (0%) risk weight.

Maturity mismatch

50. For collateralized transactions in the trading book and guaranteed transactions, the credit risk mitigating effects of such transactions will still be recognized even if a maturity mismatch occurs between the hedge and the underlying exposure, subject to appropriate adjustments.

51. For purposes of calculating risk-weighted assets, a maturity mismatch occurs when the residual maturity of a hedge is less than that of the underlying exposure.

52. The maturity of the hedge and the maturity of the underlying exposure should both be defined conservatively. For the hedge, embedded options which may reduce the term of the hedge should be taken into account so that the shortest possible effective maturity is used. Where a call is at the discretion of the guarantor/ protection seller, the maturity will always be at the first call date. If the call is at the discretion of the protection buying bank but the terms of the arrangement at origination of the hedge contain a positive incentive for the bank to call the transaction before contractual maturity, the remaining time to the first call date will be deemed to be the effective maturity. For example, where there is a step-up in cost in conjunction with a call feature or where the effective cost of cover increases over time even if credit quality remains the same or increases, the effective maturity will be the remaining time to the first call. The effective maturity of the underlying, on the other hand, should be gauged as the longest remaining time before the counterparty is scheduled to fulfill its obligation, taking into account any applicable grace period.

53. Hedges with maturity mismatches are only recognized when their original maturities are greater than or equal to one year. As a result, the maturity of hedges for exposures with original maturities of less than one (1) year must be matched to be recognized. In all cases, hedges will no longer be recognized when they have a residual maturity of three months or less.

54. When there is a maturity mismatch with recognized credit risk mitigants, the following adjustment will be applied.

$$Pa = P \times (t - 0.25)/(T - 0.25)$$

Where:

Pa = value of the credit protection adjusted for maturity mismatch

P = credit protection (e.g., collateral amount, guarantee amount) adjusted for any haircuts
t = min (T, residual maturity of the credit protection arrangement) expressed in years
T = min (5, residual maturity of the exposure) expressed in years

C. Use of third party credit assessments

55. The following third party credit assessment agencies are recognized by the BSP for regulatory capital purposes:

International credit assessment agencies:
a) Standard & Poor's;
b) Moody's;
c) Fitch Ratings; and
d) Such other rating agencies as may be approved by the Monetary Board.

Domestic credit assessment agencies:
a) PhilRatings; and
b) Such other rating agencies as may be approved by the Monetary Board.

56. The tables below set out the mapping of ratings given by the recognized credit assessment agencies for purposes of determining the appropriate risk weights:

Agency	INTERNATIONAL RATINGS						
S&P	AAA	AA+	AA	AA-	A+	A	A-
Moody's	Aaa	Aa1	Aa2	Aa3	A1	A2	A3
Fitch	AAA	AA+	AA	AA-	A+	A	A-
Agency	DOMESTIC RATINGS						
PhilRatings	AAA	Aa+	Aa	Aa-	A+	A	A-

Agency	INTERNATIONAL RATINGS						
S&P	BBB+	BBB	BBB-	BB+	BB	BB-	B+
Moody's	Baa1	Baa2	Baa3	Ba1	Ba2	Ba3	B1
Fitch	BBB+	BBB	BBB-	BB+	BB	BB-	B+
Agency	DOMESTIC RATINGS						
PhilRatings	Baa+	Baa	Baa-	Ba+	Ba	Ba-	B+

Agency	INTERNATIONAL RATINGS		
S&P	B	B-	
Moody's	B2	B3	
Fitch	B	B-	
Agency	DOMESTIC RATINGS		
PhilRatings	B	B-	

57. The BSP will issue the mapping of ratings of other rating agencies as soon as it is recognized by the BSP for regulatory capital purposes.

National Rating Systems

58. With prior BSP approval, international credit rating agencies may have national rating systems developed exclusively for use in the Philippines using the Philippine sovereign as reference highest credit quality anchor.

Multiple Assessments

59. If an exposure has only one rating by any of the BSP recognized credit assessment agencies, that rating shall be used to determine the risk weight of the exposure; in cases where there are two or more ratings which map into different risk

weights, the higher of the two lowest risk weights should be used.

Issuer versus issue assessments

60. Any reference to credit rating shall refer to issue-specific rating; the issuer rating may be used only if the exposure being risk-weighted is:

a) an unsecured senior obligation of the issuer and is of the same denomination applicable to the issuer rating (e.g., local currency issuer rating may be used for risk weighting local currency denominated senior claims);

b) short-term; and

c) in cases of guarantees.

61. For loans, risk weighting shall depend on either the rating of the borrower or the rating of the unsecured senior obligation of the borrower: *Provided*, That in case of the latter, the loan is of the same currency denomination as the unsecured senior obligation.

Domestic versus international debt issuances

62. Domestic debt issuances may be rated by BSP-recognized domestic credit assessment agencies or by international credit assessment agencies which have developed a national rating system acceptable to the BSP. Internationally-issued debt obligations shall be rated by BSP-recognized international credit assessment agencies only.

Level of application of the assessment

63. External credit assessments for one entity within a corporate group cannot be used to proxy for the credit assessment of other entities within the same group. Such other entities should secure their own ratings.

Part IV. Credit Derivatives

1. This Part sets out the capital treatment for credit derivatives. Banks may use credit derivatives to mitigate its credit risks or to acquire credit risks. For credit derivatives that are used as credit risk mitigants (CRM), the general requirements for the use of CRM techniques in paragraphs 21 to 25, Part III.B, have to be satisfied, in addition to the specific operational requirements for credit derivatives in paragraphs 8 to 14.

2. The contents of this Part are just the general rules to be followed in computing capital requirements for credit derivatives. A bank, therefore, is expected to consult the BSP-SES when there is uncertainty about the computation of capital requirements, or even about whether a given transaction should be treated under the credit derivatives framework.

A. Definitions and general terminology

3. *Credit derivative* – a contract wherein one party called the *protection buyer* or *credit risk seller* transfers the credit risk of a reference asset or assets issued by a reference entity or entities, which it may or may not own, to another party called the *protection seller* or *credit risk buyer*. In return, the protection buyer pays a premium or interest-related payments to the protection seller reflecting the underlying credit risk of the reference asset/s. Credit derivatives may refer to credit default swaps (CDS), total return swaps (TRS), and credit-linked notes (CLN) and similar products.

4. *Credit default swap* – a credit derivative wherein the protection buyer may exchange the reference asset or any deliverable obligation of the reference entity for cash equal to a specified amount, or get compensated to the extent of the difference between the par value and market value of the asset upon the occurrence of a defined credit event.

5. *Total return swap* – a credit derivative wherein the protection buyer exchanges the actual collections and

variations in the prices of the reference asset with the protection seller in return for a fixed premium.

6. *CLn* – a pre-funded credit derivative wherein the note holder acts as a protection seller while the note issuer is the protection buyer. As such, the repayment of the principal to the note holder is contingent upon the non-occurrence of a defined credit event. All references to CLNs shall be taken to generically include similar instruments, such as credit-linked deposits (CLDs).

7. *Special purpose vehicle* – refers to an entity specifically established to issue CLNs of a single, homogeneous risk class that are fully collateralized as to principal by eligible collateral instruments listed in paragraph 34, Part III.B, and which are purchased out of the proceeds of the note issuance.

B. Operational requirements for credit derivatives

8. A credit derivative must represent a direct claim on the protection seller and must be explicitly referenced to specific exposures or a pool of exposures, so that the extent of the cover is clearly defined and incontrovertible. Other than non-payment by a protection buyer of money due in respect of the credit derivative contract, it must be irrevocable; there must be no clause in the contract that would allow the protection seller unilaterally to cancel the credit cover or that would increase the effective cost of cover as a result of deteriorating credit quality in the hedged exposure. It must also be unconditional; there should be no clause in the credit derivative contract outside the direct control of the protection buyer that could prevent the protection seller from being obliged to pay out in a timely manner in the event of a defined credit event.

9. The credit events specified by the contracting parties must at a minimum cover:

a) failure to pay the amounts due under terms of the underlying obligation that are in effect at the time of such failure (with a grace period that is closely in line with the grace period in the underlying obligation);

b) bankruptcy, insolvency or inability of the obligor to pay its debts, or its failure or admission in writing of its inability generally to pay its debts as they become due, and analogous events; and

c) restructuring of the underlying obligation involving forgiveness or postponement of principal, interest or fees that results in a credit loss event (i.e., charge-off, specific provision or other similar debit to the profit and loss account).

10. The credit derivative shall not terminate prior to expiration of any grace period required for a default on the underlying obligation to occur as a result of a failure to pay, subject to the provisions of paragraph 52 of Part III.B.

11. Credit derivatives allowing for cash settlement are recognized for capital purposes insofar as a robust valuation process is in place in order to estimate loss reliably. There must be a clearly specified period for obtaining post-credit event valuations of the underlying obligation.

12. If the protection buyer's right or ability to transfer the underlying obligation to the protection seller is required for settlement, the terms of the underlying obligation must provide that any required consent to such transfer may not be unreasonably withheld.

13. The identity of the parties responsible for determining whether a credit event has occurred must be clearly defined. This determination must not be the sole responsibility of the protection seller. The bank as protection buyer must have the right/ability to inform the protection seller of the occurrence of a credit event.

14. Asset mismatches (underlying obligation is different from the obligation

used for purposes of determining cash settlement or the deliverable obligation, or from the obligation used for purposes of determining whether a credit event has occurred) are permissible if:

a) the obligation used for purposes of determining cash settlement or the deliverable obligation, or the obligation used for purposes of determining whether a credit event has occurred ranks *pari passu* with or is junior to the underlying obligation; and

b) both obligations share the same obligor (i.e., the same legal entity) and legally enforceable cross-default or cross-acceleration clauses are in place.

C. Capital treatment for protection buyers

15. A bank that enters into a credit derivative transaction as a protection buyer in order to hedge an existing exposure in the banking book may only get capital relief if all the general requirements for the use of CRM techniques in paragraphs 21 to 25, Part III.B and the conditions in paragraphs 8 to 14 are satisfied. In addition, only the eligible guarantors listed in paragraph 47, Part III.B are considered as eligible protection sellers.

16. If all of the conditions in paragraph 15 are satisfied, banks that are protection buyers may apply the risk weight of the protection seller to the protected portion of the exposure being hedged. The risk weight of the protection seller should therefore be lower than the risk weight of the exposure being hedged for capital relief to be recognized. Exposures that are protected through the issuance of CLNs will be treated as transactions collateralized by cash and a zero percent (0%) risk weight is applied to the protected portion. The uncovered portion shall retain the risk weight of the bank's underlying counterparty.

17. The protected portion of an exposure is measured as follows:

a) The fixed amount, if such is to be paid upon the occurrence of a credit event; or

b) The notional value of the contract if either (1) par is to be paid in exchange for physical delivery of the reference asset, or (2) par less market value of the asset is to be paid upon the occurrence of a credit event.

18. A bank may obtain credit protection for a basket of reference entities where the contract terminates and pays out on the first entity to default. In this case, the bank may substitute the risk weight of the protection seller for the risk weight of the asset within the basket with the lowest risk-weighted amount, but only if the notional amount is less than or equal to the notional amount of the credit derivative.

19. Where the contract terminates and pays out on the n^{th} (other than the first) entity to default, the bank will only be able to recognize any reductions in the risk weight of the underlying asset if $(n-1)^{th}$ default-protection has also been obtained or when n-1 of the assets within the basket has already defaulted.

20. Where the contract is referenced to entities in the basket proportionately, reductions in the risk weight will only apply to the extent of the underlying asset's share of protection in the contract.

21. When a bank conducts an internal hedge using a credit derivative (i.e., hedging the credit risk of an exposure in the banking book with a credit derivative booked in the trading book), in order for the bank to receive any reduction in the capital requirement for the exposure in the banking book, the credit risk in the trading book must be transferred to an outside third party (i.e., an eligible protection seller).

22. Where a bank buys credit protection through a TRS and records the net payments received on the swap as net income, but does not record offsetting

deterioration in the value of the asset that is protected (either through reductions in fair value or by an addition to reserves), the credit protection will not be recognized.

23. Materiality thresholds on payments below which no payment is made in the event of loss are equivalent to retained first loss positions and must be deducted in full from the capital of the bank buying the credit protection.

24. Where the credit protection is denominated in a currency different from that in which the exposure is denominated – i.e., there is a currency mismatch – the protected portion of the exposure will be reduced by the application of a haircut, as follows:

$$Ga = G \times (1 - H_{fx})$$

Where:

Ga = adjusted protected portion of the exposure

G = protected portion of the exposure prior to haircut

H_{fx} = haircut appropriate for currency mismatch between the credit protection and underlying obligation set at eight percent (8%) (based on a 10-business day holding period and daily marking to market)

25. Where a maturity mismatch occurs between the credit protection and the underlying exposure, the protected portion of the exposure adjusted for maturity mismatch will be computed according to paragraph 50 to 54, Part III.B.

D. Capital treatment for protection sellers

26. Where a bank is a protection seller in a CDS or TRS transaction, it must calculate a capital requirement on the reference asset as if it were a direct investor in the reference asset. The risk weight of the reference asset is multiplied by the nominal amount of the protection provided by the credit derivative to obtain the risk-weighted exposure.

27. For a bank holding a CLN, credit exposure is acquired on two fronts. As such, the on-balance sheet exposure arising from the note should be weighted by adding the risk weights of the reference entity and the risk weight of the note issuer. The amount of exposure is the carrying amount of the note. If the CLN principal is fully collateralized by an eligible collateral listed in paragraph 34, Part III.B, and which satisfies the requirements in paragraphs 27 to 31, Part III.B, the risk weight of the note issuer is substituted with the risk weight associated with the relevant collateral.

28. When the credit derivative is referenced to a basket of reference entities and the contract terminates and pays out on the first entity to default in the basket, capital should be held to consider the cumulative risk of all the reference entities in the basket. This means that the risk weights of all the reference entities are added up and multiplied by the amount of the protection provided by the credit derivative to obtain the risk-weighted exposure to the basket. However, the risk-weighted exposure is capped at ten (10) times the protection provided under the contract. Accordingly, the maximum capital charge is 100% of the protection provided under the contract. The multiplier ten (10) is the reciprocal of the BSP-required minimum CAR of ten percent (10%). For CLNs, the risk weight of the issuer is likewise included in the summing of the risk weights.

29. When the contract terminates and pays out on the n^{th} (other than the first) entity to default, the treatment above shall apply except that in aggregating the risk weights of the reference entities, the risk weight/s of the n-1 lowest risk-weighted entity/ies is/are excluded from the computation. For CLNs, the risk weight of the issuer is likewise included in the summing of the risk weights.

30. When a first or an n^{th}-to-default credit derivative has an external credit rating acceptable to the BSP, the risk weight in paragraph 21, Part V.F will be applied.

31. A contract that is referenced to entities in the basket proportionately should be risk-weighted according to each reference entity's share of protection under the contract.

E. Credit derivatives in the trading book

32. The following describes the positions to be reported for credit derivative transactions for purposes of calculating specific risk and general market risk charges under the standardized approach.

33. A CDS creates a notional position in the specific risk of the reference obligation. A TRS creates notional positions on the specific and general market risks of the reference obligation, and an opposite notional position on a zero coupon government security representing the fixed payments or premium under the TRS. A CLN creates a notional position in the specific risk of the reference obligation, a position on the specific risk associated with the issuer, and a position on the general market risk of the note.

Specific risk

34. The specific risk position/s on the reference obligation/s created by credit derivatives are reported as short positions by protection buyers and long positions by protection sellers. In addition, holders of CLNs should report a long position on the specific risk of the note issuer.

35. The protection buyer in a first-to-default transaction should report a short position in the reference obligation with the lowest specific risk charge. A protection buyer in an n^{th} (other than the first)-to-default transaction shall only be allowed to report a short position in a reference obligation only if n-1 obligations in the reference basket has/have already defaulted.

36. When a credit derivative is referenced to multiple entities and the contract terminates and pays out on the first obligation to default in the basket, the transaction should be reported by the protection seller as long positions in each of the reference obligations in the basket. A CLN should likewise be reported as a long position on the note issuer. The total capital charge is capped at the notional amount of the derivative or, in the case of a CLN, the carrying amount of the note.

37. When the contract terminates and pays out on the n^{th} (other than the first) entity to default in the basket, the treatment above shall apply except that the protection seller may exclude the long position/s on n-1 reference obligations with the lowest risk-weighted exposures in its report. A CLN should likewise be reported as a long position on the note issuer. The total capital charge is capped at the notional amount of the derivative or, in the case of a CLN, the carrying amount of the note.

38. When an n^{th}-to-default credit derivative has an external credit rating acceptable to the BSP, the specific risk weights in Part VI.B will be applied.

39. When the contract is referenced to multiple obligations under a proportionate structure, positions in the reference obligations should be reported according to their respective proportions in the contract.

General market risk

40. A protection buyer/seller in a TRS should report a short/long notional position on the reference obligation and a long/short notional position on a zero coupon government security representing the fixed payment under the contract.

41. A protection buyer/seller in a CLN should report a short/long position on the note.

Counterparty credit risk

42. CDS and TRS transactions in the trading book attract counterparty credit risk charges. A five percent (5%) add-on factor for the computation of the potential future credit exposure shall be used by both protection buyers and protection sellers if the reference obligation has an external credit rating of at least BBB- or its equivalent. A ten percent (10%) add-on factor applies to all other reference obligations. However, a protection seller in a CDS shall only be subject to the add-on factor if it is subject to closeout upon the insolvency of the protection buyer while the underlying is still solvent. The add-on in this case should be capped to the amount of unpaid premiums.

43. Where the credit derivative is a first to default transaction, the add-on will be determined by the lowest credit quality underlying in the basket, i.e., if there are any non-investment grade or unrated items in the basket, the ten percent (10%) add-on should be used. For second and subsequent to default transactions, underlying assets should continue to be allocated according to the credit quality, i.e., the second lowest credit quality will determine the add-on for a second to default transaction, etc.

44. Where the credit derivative is referenced proportionately to multiple obligations, the add-on factor will follow the add-on factor applicable for the obligation with the biggest share. If the protection is equally proportioned, the highest add-on factor should be used.

Part V. Securitization

1. Banks must apply the securitization framework for determining regulatory capital requirements on their securitization exposures. Securitization exposures can include but are not restricted to the following: asset-backed securities, mortgage-backed securities, credit enhancements, liquidity facilities, interest rate or currency swaps, and credit derivatives. Underlying instruments in the pool being securitized may include but are not restricted to the following: loans, commitments, asset-backed and mortgage-backed securities, corporate bonds, equity securities, and private equity investments.

2. Since securitizations may be structured in many different ways, the capital treatment of a securitization exposure must be determined on the basis of its economic substance rather than its legal form. The contents of this Part are just the general rules to be followed in computing capital requirements for securitization exposures. A bank should therefore consult the BSP-SES when there is uncertainty about the computation of capital requirements, or even about whether a given transaction should be considered a securitization.

A. Definitions and general terminology

3. *Traditional securitization* – a structure where the cash flow from an underlying pool of exposures is used to service at least two (2) different stratified risk positions or tranches reflecting different degrees of credit risk. Payments to the investors depend upon the performance of the specified underlying exposures, as opposed to being derived from an obligation of the entity originating those exposures. The stratified/tranched structures that characterize securitizations differ from ordinary senior/subordinated debt instruments in that junior securitization tranches can absorb losses without interrupting contractual payments to more senior tranches, whereas subordination in a senior/subordinated debt structure is a matter of priority of rights to the proceeds of liquidation.

4. *Synthetic securitization* – a structure with at least two (2) different stratified risk positions or tranches that reflect different degrees of credit risk where credit risk of an underlying pool of

exposures is transferred, in whole or in part, through the use of funded (e.g., credit-linked notes) or unfunded (e.g., credit default swaps) credit derivatives or guarantees that serve to hedge the credit risk of the portfolio. Accordingly, the investors' potential risk is dependent upon the performance of the underlying pool.

5. *Originating bank* – a bank that originates directly or indirectly underlying exposures included in the securitization.

6. *Clean-up call* – an option that permits the securitization exposures to be called before all of the underlying exposures or securitization exposures have been repaid. In the case of traditional securitizations, this is generally accomplished by repurchasing the remaining securitization exposures once the pool balance or outstanding securities have fallen below some specified level. In the case of a synthetic transaction, the clean-up call may take the form of a clause that extinguishes the credit protection.

7. *Credit enhancement* – a contractual arrangement in which the bank retains or assumes a securitization exposure and, in substance, provides some degree of added protection to other parties to the transaction.

8. *Early amortization provisions* – mechanisms that, once triggered, allow investors to be paid out prior to the originally stated maturity of the securities issued. For risk-based capital purposes, an early amortization provision will be considered either controlled or non-controlled. A controlled early amortization provision must meet all of the following conditions:

a) The bank must have an appropriate capital/liquidity plan in place to ensure that it has sufficient capital and liquidity available in the event of an early amortization;

b) Throughout the duration of the transaction, including the amortization period, there is the same pro rata sharing of interest, principal, expenses, losses and recoveries based on the bank's and investors' relative shares of the receivables outstanding at the beginning of each month;

c) The bank must set a period for amortization that would be sufficient for at least ninety percent (90%) of the total debt outstanding at the beginning of the early amortization period to have been repaid or recognized as in default; and

d) The pace of repayment should not be any more rapid than would be allowed by straight-line amortization over the period set out in criterion (c).

An early amortization provision that does not satisfy the conditions for a controlled early amortization provision will be treated as non-controlled early amortization provision.

9. *Eligible liquidity facilities* – an off-balance sheet securitization exposure shall be treated as an eligible liquidity facility if the following minimum requirements are satisfied:

a) The facility documentation must clearly identify and limit the circumstances under which it may be drawn. Draws under the facility must be limited to the amount that is likely to be repaid fully from the liquidation of the underlying exposures and any seller-provided credit enhancements. In addition, the facility must not cover any losses incurred in the underlying pool of exposures prior to a draw, or be structured such that draw-down is certain (as indicated by regular or continuous draws);

b) The facility must be subject to an asset quality test that precludes it from being drawn to cover credit risk exposures that are considered non-performing under existing BSP regulations. In addition, liquidity facilities should only fund exposures that are externally rated investment grade at the time of funding;

c) The facility cannot be drawn after all applicable (e.g., transaction-specific and program-wide) credit enhancements from which the liquidity would benefit have been exhausted; and

d) Repayment of draws on the facility (i.e., assets acquired under a purchase agreement or loans made under a lending agreement) must not be subordinated to any interests of any note holder in the program or subject to deferral or waiver.

10. *Eligible servicer cash advance facilities* – cash advance that may be provided by servicers to ensure an uninterrupted flow of payments to investors. The servicer should be entitled to full reimbursement and this right is senior to other claims on cash flows from the underlying pool of exposures.

11. *Excess spread* – generally defined as gross finance charge collections and other income received by the trust or special purpose entity (SPE, specified in paragraph 13) minus certificate interest, servicing fees, charge-offs, and other senior trust or SPE expenses.

12. *Implicit support* – arises when a bank provides support to a securitization in excess of its predetermined contractual obligation.

13. *Special purpose entity* – a corporation, trust, or other entity organized for a specific purpose, the activities of which are limited to those appropriate to accomplish the purpose of the SPE, and the structure of which is intended to isolate the SPE from the credit risk of an originator or seller of exposures. SPEs are commonly used as financing vehicles in which exposures are sold to a trust or similar entity in exchange for cash or other assets funded by debt issued by the trust.

B. Operational requirements for the recognition of risk transference in traditional securitizations

14. An originating bank may exclude securitized exposures from the calculation of risk-weighted assets only if all of the following conditions have been met. Banks meeting these conditions, however, must still hold regulatory capital against any securitization exposures they retain.

a) Significant credit risk associated with the securitized exposures has been transferred to third parties.

b) The transferor does not maintain effective or indirect control over the transferred exposures. The assets are legally isolated from the transferor in such a way (e.g., through the sale of assets or through subparticipation) that the exposures are put beyond the reach of the transferor and its creditors, even in bankruptcy or receivership. These conditions must be supported by an opinion provided by a qualified legal counsel.

The transferor is deemed to have maintained effective control over the transferred credit risk exposures if it:

i. is able to repurchase from the transferee the previously transferred exposures in order to realize their benefits; or

ii. is obligated to retain the risk of the transferred exposures.

The transferor's retention of servicing rights to the exposures will not necessarily constitute indirect control of the exposures.

c) The securities issued are not obligations of the transferor. Thus, investors who purchase the securities only have claim to the underlying pool of exposures.

d) The transferee is an SPE and the holders of the beneficial interests in that entity have the right to pledge or exchange them without restriction.

e) Clean-up calls must satisfy the conditions set out in paragraph 17.

f) The securitization does not contain clauses that (i) require the originating bank to alter systematically the underlying exposures such that the pool's weighted average credit quality is improved unless this is achieved by selling assets to independent and unaffiliated third parties at market prices; (ii) allow for increases in a retained first loss position or credit enhancement provided by the originating bank after the transaction's inception; or (iii) increase the yield payable to parties other than the originating bank, such as investors

and third-party providers of credit enhancements, in response to a deterioration in the credit quality of the underlying pool.

C. Operational requirements for the recognition of risk transference in synthetic securitizations

15. For synthetic securitizations, the use of CRM techniques (i.e., collateral, guarantees and credit derivatives) for hedging the underlying exposure may be recognized for risk-based capital purposes only if the conditions outlined below are satisfied:

a) Credit risk mitigants must comply with the requirements as set out in Part III.B and Part IV of this Framework.

b) Eligible collateral is limited to that specified in paragraph 34, Part III.B. Eligible collateral pledged by SPEs may be recognized.

c) Eligible guarantors are defined in paragraph 47, Part III.B. SPEs are not recognized as eligible guarantors in the securitization framework.

d) Banks must transfer significant credit risk associated with the underlying exposure to third parties.

e) The instruments used to transfer credit risk must not contain terms or conditions that limit the amount of credit risk transferred, such as those provided below:

i. Clauses that materially limit the credit protection or credit risk transference (e.g., significant materiality thresholds below which credit protection is deemed not to be triggered even if a credit event occurs or those that allow for the termination of the protection due to deterioration in the credit quality of the underlying exposures);

ii. Clauses that require the originating bank to alter the underlying exposures to improve the pool's weighted average credit quality;

iii. Clauses that increase the banks' cost of credit protection in response to deterioration in the pool's quality;

iv. Clauses that increase the yield payable to parties other than the originating bank, such as investors and third-party providers of credit enhancements, in response to a deterioration in the credit quality of the reference pool; and

v. Clauses that provide for increases in a retained first loss position or credit enhancement provided by the originating bank after the transaction's inception.

f) An opinion must be obtained from a qualified legal counsel that confirms the enforceability of the contracts in all relevant jurisdictions.

g) Clean-up calls must satisfy the conditions set out in paragraph 17.

16. For synthetic securitizations, the effect of applying CRM techniques for hedging the underlying exposure are treated according to Part III.B and Part IV of this Framework. In case there is a maturity mismatch, the capital requirement will be determined in accordance with paragraphs 50 to 54, Part III.B. When the exposures in the underlying pool have different maturities, the longest maturity must be taken as the maturity of the pool. Maturity mismatches may arise in the context of synthetic securitizations when, for example, a bank uses credit derivatives to transfer part or all of the credit risk of a specific pool of assets to third parties. When the credit derivatives unwind, the transaction will terminate. This implies that the effective maturity of the tranches of the synthetic securitization may differ from that of the underlying exposures. Originating banks of synthetic securitizations with such maturity mismatches must deduct all retained positions that are unrated or rated below investment grade. Accordingly, when deduction is required, maturity mismatches are not taken into account. For all other securitization exposures, the bank must apply the maturity mismatch treatment set forth in paragraphs 50 to 54, Part III.B.

D. Operational requirements and treatment of clean-up calls

17. For securitization transactions that include a clean-up call, no capital will be required due to the presence of a clean-up call if the following conditions are met: (i) the exercise of the clean-up call must not be mandatory, in form or in substance, but rather must be at the discretion of the originating bank; (ii) the clean-up call must not be structured to avoid allocating losses to credit enhancements or positions held by investors or otherwise structured to provide credit enhancement; and (iii) the clean-up call must only be exercisable when ten percent (10%) or less of the original underlying portfolio, or securities issued remain, or, for synthetic securitizations, when ten percent (10%) or less of the original reference portfolio value remains.

18. Securitization transactions that include a clean-up call that does not meet all of the criteria stated in paragraph 17 result in a capital requirement for the originating bank. For a traditional securitization, the underlying exposures must be treated as if they were not securitized. Additionally, banks must not recognize in regulatory capital any gain-on-sale, as defined in paragraph 23. For synthetic securitization, the bank purchasing protection must hold capital against the entire amount of the securitized exposures as if they did not benefit from any credit protection. Same treatment applies for synthetic securitization that incorporates a call, other than a clean-up call, that effectively terminates the transaction and the purchased credit protection on a specified date.

19. If a clean-up call, when exercised, is found to serve as a credit enhancement, the exercise of the clean-up call must be considered a form of implicit support provided by the bank and must be treated in accordance with paragraph 26.

E. Operational requirements for use of external credit assessments

20. The following operational criteria concerning the use of external credit assessments apply in the securitization framework:

a) To be eligible for risk-weighting purposes, the external credit assessment must take into account and reflect the entire amount of credit risk exposure the bank has with regard to all payments owed to it. For example, if a bank is owed both principal and interest, the assessment must fully take into account and reflect the credit risk associated with timely repayment of both principal and interest.

b) The external credit assessments must be from an eligible ECAI as recognized by the bank's national supervisor in accordance with Part III.C. An eligible credit assessment must be publicly available. In other words, a rating must be published in an accessible form and included in the ECAI's transition matrix. Consequently, ratings that are made available only to the parties to a transaction do not satisfy this requirement.

c) Eligible ECAIs must have a demonstrated expertise in assessing securitizations, which may be evidenced by strong market acceptance.

d) A bank must apply external credit assessments from eligible ECAIs consistently across a given type of securitization exposure. Furthermore, a bank cannot use the credit assessments issued by one ECAI for one or more tranches and those of another ECAI for other positions (whether retained or purchased) within the same securitization structure that may or may not be rated by the first ECAI. Where two or more eligible ECAIs can be used and these assess the credit risk of the same securitization exposure differently, paragraph 59 of Part III.C will apply.

e) Where CRM is provided directly to an SPE by an eligible guarantor defined in

paragraph 47 of Part III.B and is reflected in the external credit assessment assigned to a securitization exposure(s), the risk weight associated with that external credit assessment should be used. In order to avoid any double counting, no additional capital recognition is permitted. If the CRM provider is not an eligible guarantor, the covered securitization exposures should be treated as unrated.

f) In the situation where a credit risk mitigant is not obtained by the SPE but rather applied to a specific securitization exposure within a given structure (e.g., ABS tranche), the bank must treat the exposure as if it is unrated and then use the CRM treatment outlined in Part III.B to recognize the hedge.

F. Risk-weighting

21. The risk-weighted asset amount of a securitization exposure is computed by multiplying the amount of the position by the appropriate risk weight determined in accordance with the following table. For off-balance sheet exposures, banks must apply a credit conversion factor (CCF) and then risk weight the resultant credit equivalent amount.

Credit assessment[1]	AAA to AA-	A+ to A-	BBB+to BBB-	Below BBB- and unrated
Risk weight	20%	50%	100%	Deduction from capital (50% from Tier 1 and 50% from Tier 2)

22. The capital treatment of implicit support, liquidity facilities, securitizations of revolving exposures, and credit risk mitigants are identified separately.

23. Banks must deduct from Tier 1 capital any increase in equity capital resulting from a securitization transaction, such as that associated with expected future margin income resulting in a gain-on-sale that is recognized in regulatory capital. Such an increase in capital is referred to as a "gain-on-sale" for the purposes of the securitization framework.

24. Credit enhancing interest only, net of the amount that must be deducted from Tier 1 as in paragraph 23, are to be deducted fifty percent (50%) from Tier 1 capital and fifty percent (50%) from Tier 2 capital.

25. Deductions from capital may be calculated net of any specific provisions taken against the relevant securitization exposures.

26. When a bank provides implicit support to a securitization, it must, at a minimum, hold capital against all of the exposures associated with the securitization transaction as if they had not been securitized. Additionally, banks would not be permitted to recognize in regulatory capital any gain-on-sale, as defined in paragraph 23. Furthermore, the bank is required to disclose publicly that (a) it has provided non-contractual support and (b) the capital impact of doing so.

27. As a general rule, off-balance sheet securitization exposures will receive a CCF of 100%, except in the cases below.

28. A CCF of twenty percent (20%) and fifty percent (50%) will be applied to eligible liquidity facilities as defined in paragraph 9 above with original maturity of one year or less and more than one year, respectively. However, if an external rating of the facility itself is used for risk weighting the facility, a 100% CCF must be applied. A zero percent (0%) CCF may be applied to eligible liquidity facilities that are only available in the event of a general market disruption (i.e., whereupon more than one SPE across different transactions are unable to roll over maturing commercial paper, and that inability is not the result of an impairment in the SPE's credit quality or in the credit

[1] The notations follow the rating symbols used by Standard & Poor's. The mapping of ratings of all recognized external rating agencies is in Part III.C

quality of the underlying exposures). To qualify for this treatment, the conditions provided in paragraph 9 must be satisfied. Additionally, the funds advanced by the bank to pay holders of the capital market instruments (e.g., commercial paper) when there is a general market disruption must be secured by the underlying assets, and must rank at least *pari passu* with the claims of holders of the capital market instruments.

29. A CCF of zero percent (0%) will be applied to undrawn amount of eligible servicer cash advance facilities, as defined in paragraph 10 above, that are unconditionally cancellable without prior notice.

30. An originating bank is required to hold capital against the investors' interest (i.e., against both the drawn and undrawn balances related to the securitized exposures) when:

a) It sells exposures into a structure that contains an early amortization feature; and

b) The exposures sold are of a revolving nature. These involve exposures where the borrower is permitted to vary the drawn amount and repayments within an agreed limit under a line of credit (e.g., credit card receivables and corporate loan commitments).

31. Originating banks, though, are not required to calculate a capital requirement for early amortizations in the following situations:

a) Replenishment structures where the underlying exposures do not revolve and the early amortization ends the ability of the bank to add new exposures;

b) Transactions of revolving assets containing early amortization features that mimic term structures (i.e., where the risk of the underlying facilities does not return to the originating bank);

c) Structures where a bank securitizes one or more credit line(s) and where investors remain fully exposed to future draws by borrowers even after an early amortization event has occurred; and

d) The early amortization clause is solely triggered by events not related to the performance of the securitized assets or the selling bank, such as material changes in tax laws or regulations.

32. As described below, the CCFs depend upon whether the early amortization repays investors through a controlled or non-controlled mechanism. They also differ according to whether the securitized exposures are uncommitted retail credit lines (e.g., credit card receivables) or other credit lines (e.g., revolving corporate facilities). A line is considered uncommitted if it is unconditionally cancelable without prior notice.

33. For uncommitted retail credit lines (e.g., credit card receivables) that have either controlled or non-controlled early amortization features, banks must compare the three-month average excess spread defined in paragraph 11 to the point at which the bank is required to trap excess spread as economically required by the structure (i.e., excess spread trapping point). In cases where such a transaction does not require excess spread to be trapped, the trapping point is deemed to be 4.5 percentage points.

34. The bank must divide the excess spread level by the transaction's excess spread trapping point to determine the appropriate segments and apply the corresponding conversion factors, as outlined in the following tables:

	Controlled		Non-controlled	
	3-month average excess spread-credit conversion factor (CCF)	**Credit conversion factor (CCF)**	**3-month average excess spread-credit conversion factor (CCF)**	**Credit conversion factor (CCF)**
	Uncommitted	**Committed**	**Uncommitted**	**Committed**
Retail credit lines	133.33% of trapping point or more – 0% CCF less than 133.33% to 100% of trapping point – 1% CCF less than 100% to 75% of trapping point – 2% CCF less than 75% to 50% of trapping point - 10% CCF less than 50% to 25% of trapping point - 20% CCF less than 25% of trapping point - 40%	90% CCF	133.33% of trapping point or more – 0% CCF less than 133.33% to 100% of trapping point – 5% CCF less than 100% to 75% of trapping point – 15% CCF less than 75% to 50% of trapping point - 50% CCF less than 50% of trapping point - 100% CCF	100% CCF
Non-retail credit lines	90% CCF	90% CCF	100% CCF	100%CCF

35. All other securitized revolving exposures with controlled and non-controlled early amortization features will be subject to CCFs of ninety percent (90%) and 100%, respectively, against the off-balance sheet exposures.

36. The CCF will be applied to the amount of the investors' interest. The resultant credit equivalent amount shall then be applied a risk weight applicable to the underlying exposure type, as if the exposures had not been securitized.

37. For a bank subject to the early amortization treatment, the total capital charge for all of its positions will be subject to a maximum capital requirement (i.e., a 'cap') equal to the greater of (i) that required for retained securitization exposures, or (ii) the capital requirement that would apply had the exposures not been securitized. In addition, banks must deduct the entire amount of any gain-on-sale and credit enhancing interest only arising from the securitization transaction in accordance with paragraphs 23 and 25.

G. Credit risk mitigation

38. The treatment below applies to a bank that has obtained or given a credit risk mitigant on a securitization exposure. Credit risk mitigants include collateral, guarantees, and credit derivatives. Collateral in this context refers to that used to hedge the credit risk of a securitization exposure rather than the underlying exposures of the securitization transaction.

Collateral

39. Eligible collateral is limited to that recognized in paragraph 34, Part III.B. Collateral pledged by SPEs may be recognized.

Guarantees and credit derivatives

40. Credit protection provided by the entities listed in paragraph 47, Part III.B may be recognized. SPEs cannot be recognized as eligible guarantors.

41. Where guarantees or credit derivatives fulfill the minimum operational requirements as specified in Part III.B and Part IV, respectively, banks can take account of such credit protection in calculating capital requirements for securitization exposures.

42. Capital requirements for the collateralized or guaranteed/protected portion will be calculated according to Part III.B and Part IV.

43. A bank other than the originator providing credit protection to a securitization exposure must calculate a capital requirement on the covered exposure as if it were an investor in that securitization. A bank providing protection to an unrated credit enhancement must treat the credit protection provided as if it were directly holding the unrated credit enhancement.

Maturity mismatches

44. For the purpose of setting regulatory capital against a maturity mismatch, the capital requirement will be determined in accordance with paragraphs 50 to 54, Part III.B, except for synthetic securitizations which will be determined in accordance with paragraph 16.

Part VI. Market risk-weighted assets

1. Market risk is defined as the risk of losses in on- and off-balance sheet positions arising from movements in market prices. The risks addressed in these guidelines are:

a) The risks pertaining to interest rate-related instruments and equities in the trading book; and

b) Foreign exchange risk throughout the bank.

A. Definition of the trading book

2. A trading book consists of positions in financial instruments held either with trading intent or in order to hedge other elements of the trading book. To be eligible for trading book capital treatment, financial instruments must either be free of any restrictive covenants on their tradability or able to be hedged completely. In addition, positions should be frequently and accurately valued, and the portfolio should be actively managed.

3. A financial instrument is any contract that gives rise to both a financial asset of one entity and a financial liability or equity instrument of another entity. Financial instruments include both primary financial instruments (or cash instruments) and derivative financial instruments. A financial asset is any asset that is cash, the right to receive cash or another financial asset; or the contractual right to exchange financial assets on potentially favorable terms, or an equity instrument. A financial liability is the contractual obligation to deliver cash or another financial asset or to exchange financial liabilities under conditions that are potentially unfavorable.

4. Positions held with trading intent are those held intentionally for short-term resale and/or with the intent of benefiting from actual or expected short-term price movements or to lock in arbitrage profits,

and may include for example proprietary positions, positions arising from client servicing (e.g. matched principal brokering) and market making.

5. The following will be the basic requirements for positions eligible to receive trading book capital treatment:

a) Clearly documented trading strategy for the position/instrument or portfolios, approved by senior management (which would include expected holding horizon);

b) Clearly defined policies and procedures for the active management of the position, which must include:

i. positions are managed on a trading desk;

ii. position limits are set and monitored for appropriateness;

iii. dealers have the autonomy to enter into/manage the position within agreed limits and according to the agreed strategy;

iv. positions are marked to market at least daily, and when marking to model the parameters must be assessed on a daily basis;

v. positions are reported to senior management as an integral part of the institution's risk management process; and

vi. positions are actively monitored with reference to market information sources (assessment should be made of the market liquidity or the ability to hedge positions or the portfolio risk profiles). This would include assessing the quality and availability of market inputs to the valuation process, level of market turnover, sizes of positions traded in the market, etc.

c) Clearly defined policy and procedures to monitor the positions against the bank's trading strategy including the monitoring of turnover and stale positions in the bank's trading book.

6. The documentations of the basic requirements of paragraph 5 should be submitted to the BSP.

7. In addition to the above documentation requirements, the bank should also submit to the BSP a documentation of its systems and controls for the prudent valuation of positions in the trading book including the valuation methodologies.

B. Measurement of capital charge

8. The market risk capital charge shall be computed according to the methodology set under Subsec. 1115.2 of the MORB, subject to certain modifications as outlined in the succeeding paragraphs.

9. The specific risk weights for trading book positions in debt securities and debt derivatives shall depend on the third party credit assessment of the issue or the type of issuer, as may be appropriate, as follows:

Credit ratings of debt securities/derivatives issued by sovereigns[1]	**Credit ratings of debt securities/derivatives issued by MDBs**	**Credit ratings of debt securities/derivatives issued by other entities**	**Unadjusted specific risk weight**
Php-denominated debt securities/derivatives issued by the Philippine NG and BSP			0.00%
LGU Bonds covered by Deed of Assignment of Internal Revenue Allotment and guaranteed by LGU Guarantee Corporation			4.00%
AAA to AA-	AAA		0.00%
A+ to BBB-	AA+ to BBB-	AAA to BBB-	
Residual maturity ≤ 6 months	Residual maturity ≤ 6 months	Residual maturity ≤ 6 months	0.25%
Residual maturity > 6 months, ≤ 24 months	Residual maturity > 6 months, ≤ 24 months	Residual maturity > 6 months, ≤ 24 months	1.00%
Residual maturity > 24 months	Residual maturity > 24 months	Residual maturity > 24 months	1.60%
		All other debt securities/ derivatives	8.00%

[1] The notations follow the rating symbols used by Standard & Poor's. The mapping of ratings of all recognized external rating agencies is in Part III.C. For purposes of this framework, debt securities/derivatives issued by sovereigns include foreign currency denominated debt securities/derivatives issued by the Philippine NG.

10. Foreign currency denominated debt securities/derivatives issued by the Philippine NG and BSP[1] shall be risk-weighted according to the table above: *Provided*, That only one-third (1/3) of the applicable risk weight shall be applied from 01 July 2007, two-thirds (2/3) from 01 January 2008, and the full risk weight from 01 January 2009.

11. A security, which is the subject of a repo-style transaction, shall be treated as if it were still owned by the seller/lender of the security, i.e., to be reported by the seller/lender.

12. In addition to capital charge for specific and general market risk, a credit risk capital charge should be applied to banks' counterparty exposures in repo-style transactions and OTC derivatives contracts. The computation of the credit risk capital charge for counterparty exposures arising from trading book positions are discussed in paragraphs 35 to 41 of Part III.B.

(As amended by Circular No. 605 dated 05 March 2008)

C. Measurement of risk-weighted assets

13. Market risk-weighted assets are determined by multiplying the market risk capital charge by ten (10) [i.e., the reciprocal of the minimum capital ratio of ten percent (10%)].

Part VII. Operational risk-weighted assets

A. Definition of operational risk

1. Operational risk is defined as the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events. This definition includes legal risk, but excludes strategic and reputational risk.

2. Banks should be guided by the Basel Committee on Banking Supervision's recommendations on *Sound Practices for the Management and Supervision of Operational Risk* (February 2003). The same may be downloaded from the BIS website (www.bis.org).

B. Measurement of capital charge

3. In computing for the operational risk capital charge, Banks may use either the basic indicator approach or the standardized approach.

4. Under the basic indicator approach, banks must hold capital for operational risk equal to fifteen percent (15%) of the average gross income over the previous three (3) years of positive annual gross income. Figures for any year in which annual gross income is negative or zero should be excluded from both the numerator and denominator when calculating the average.

5. Banks that have the capability to map their income accounts into the various business lines given in paragraph 7 may use the standardized approach subject to prior BSP approval[2]. In order to qualify for use of the standardized approach, a bank must satisfy BSP that, at a minimum:

a) Its board of directors and senior management are actively involved in the oversight of the operational risk management framework;

b) It has an operational risk management system that is conceptually sound and is implemented with integrity; and

c) It has sufficient resources in the use of the approach in the major business lines as well as the control and audit areas.

6. Operational risk capital charge is calculated as the three (3)-year average of the simple summation of the regulatory capital charges across each of the business lines in each year. In any given year, negative capital charges (resulting from negative gross income) in any business line may offset positive capital charges in other

[1] Warrants paired with ROP Global Bonds shall be exempted from capital charge for market risk only to the extent of bank's holdings of bonds paired with warrants equivalent to not more than fifty (50%) of total qualifying capital, as defined under Part II of this Appendix.

[2] Refer to *Appendix Q-46b* for the Guidelines on the Use of the Standardized Approach in Computing the Capital Charge for Operational Risk

business lines without limit. However, where the aggregate capital charge across all business lines within a given year is negative, then figures for that year shall be excluded from both the numerator and denominator.

7. The business lines and their corresponding beta factors are listed below:

Business lines		Activity Groups	Beta factors
Level 1	**Level 2**		
Corporate finance	Corporate Finance	Mergers and acquisitions, underwriting, privatizations, securitization, research, debt (government, high yield), equity, syndications, IPO, secondary private placements	18%
	Municipal/Government Finance		
	Advisory Services		
Trading and Sales	Sales	Fixed income, equity, foreign exchanges, commodities, credit, funding, own position securities, lending and repos, brokerage, debt, prime brokerage	18%
	Market Making		
	Proprietary Positions		
	Treasury		
Retail Banking	Retail Banking	Retail lending and deposits, banking services, trust and estates	12%
	Private Banking	Private lending and deposits, banking services, trust and estates, investment advice	
	Card Services	Merchant/commercial/corporate cards, private labels and retail	
Commercial Banking	Commercial Banking	Project finance, real estate, export finance, trade finance, factoring, leasing, lending, guarantees, bills of exchange	15%
Payment and Settlement	External Clients	Payments and collections, funds transfer, clearing and settlement	18%
Agency Services	Custody	Escrow, depository receipts, securities lending (customers) corporate actions	15%
	Corporate Agency	Issuer and paying agents	
	Corporate Trust		
Asset Management	Discretionary Fund Management	Discretionary and non-discretionary fund management, whether pooled, segregated, retail, institutional, closed, open, private equity	12%
	Non-Discretionary Fund Management		
Retail Brokerage	Retail brokerage	Execution and full service	12%

8. Gross income, for the purpose of computing for operational risk capital charge, is defined as net interest income plus non-interest income. This measure should:

a) be gross of any provisions for losses on accrued interest income from financial assets;

b) be gross of operating expenses, including fees paid to outsourcing service providers;

c) include fees and commissions;

d) exclude gains/(losses) from the sale/redemption/derecognition of non-trading financial assets and liabilities;

e) exclude gains/(losses) from sale/derecognition of non-financial assets; and

f) include other income (i.e., rental income, miscellaneous income, etc.)

C. Measurement of risk-weighted assets

9. The resultant operational risk capital charge is to be multiplied by 125% before multiplying by ten (10) [i.e., the reciprocal of the minimum capital ratio of ten percent (10%)].

(As amended by M-2007-019 dated 21 June 2007)

Part VIII. Disclosures in the Annual Reports and Published Statement of Condition

1. This section lists the specific information that banks have to disclose, at

a minimum, in their Annual Reports, except Item *"h"*, paragraph 4 which should also be disclosed in banks' quarterly Published Statement of Condition. These enhanced disclosures shall commence with Annual Reports for financial year 2007 and quarterly published statement of condition from end-September 2007.

2. Full compliance of these disclosure requirements is a prerequisite before banks can obtain any capital relief (i.e., adjustments in the risk weights of collateralized or guaranteed exposures) in respect of any credit risk mitigation techniques.

A. Capital structure and capital adequacy

3. The following information with regard to banks' capital structure and capital adequacy shall be disclosed in banks' Annual Reports, except Item *"h"* below which should also be disclosed in banks' quarterly published statement of condition:

a) Tier 1 capital and a breakdown of its components (including deductions solely from Tier 1);

b) Tier 2 capital and a breakdown of its components;

c) Deductions from Tier 1 fifty percent (50%) and Tier 2 fifty percent (50%) capital;

d) Total qualifying capital;

e) Capital requirements for credit risk (including securitization exposures);

f) Capital requirements for market risk;

g) Capital requirements for operational risk; and

h) Total and Tier 1 CAR on both solo and consolidated bases.

B. Risk exposures and assessments

4. For each separate risk area (credit, market, operational, interest rate risk in the banking book), banks must describe their risk management objectives and policies, including:

a) Strategies and processes;

b) The structure and organization of the relevant risk management function;

c) The scope and nature of risk reporting and/or measurement systems; and

d) Policies for hedging and/or mitigating risk, and strategies and processes for monitoring the continuing effectiveness of hedges/mitigants.

Credit risk

5. Aside from the general disclosure requirements stated in paragraph 4, the following information with regard to credit risk have to be disclosed in banks' Annual Reports:

a) Total credit risk exposures (i.e., principal amount for on-balance sheet and credit equivalent amount for off-balance sheet, net of specific provision) broken down by type of exposures as defined in Part III;

b) Total credit risk exposure after risk mitigation, broken down by:

i. type of exposures as defined in Part III; and

ii. risk buckets, as well as those that are deducted from capital;

c) Total credit risk-weighted assets broken down by type of exposures as defined in Part III;

d) Names of external credit assessment institutions used, and the types of exposures for which they were used;

e) Types of eligible credit risk mitigants used including credit derivatives;

f) For banks with exposures to securitization structures, aside from the general disclosure requirements stated in paragraph 4, the following minimum information have to be disclosed:

i. Accounting policies for these activities;

ii. Total outstanding exposures securitized by the bank; and

iii. Total amount of securitization exposures retained or purchased, broken down by exposure type;

g) For banks that provide credit protection through credit derivatives, aside

from the general disclosure requirements stated in paragraph 4, total outstanding amount of credit protection given by the bank broken down by type of reference exposures should also be disclosed; and

h) For banks with investments in other types of structured products, aside from the general disclosure requirements stated in paragraph 4, total outstanding amount of other types of structured products issued or purchased by the bank broken down by type should also be disclosed.

Market risk

6. Aside from the general disclosure requirements stated in paragraph 4, the following information with regard to market risk have to be disclosed in banks' Annual Reports:

a) Total market risk-weighted assets broken down by type of exposures (interest rate, equity, foreign exchange, and options); and

b) For banks using the internal models approach, the following information have to be disclosed:

i. The characteristics of the models used;

ii. A description of stress testing applied to the portfolio;

iii. A description of the approach used for backtesting/validating the accuracy and consistency of the internal models and modeling processes;

iv. The scope of acceptance by the BSP; and

v. A comparison of VaR estimates with actual gains/losses experienced by the bank, with analysis of important outliers in backtest results.

Operational risk

7. Aside from the general disclosure requirements stated in paragraph 4, banks have to disclose their operational risk-weighted assets in their Annual Reports.

Interest rate risk in the banking book

8. Aside from the general disclosure requirements stated in paragraph 4, the following information with regard to interest rate risk in the banking book have to be disclosed in banks' Annual Reports:

a) Internal measurement of interest rate risk in the banking book, including assumptions regarding loan prepayments and behavior of non-maturity deposits, and frequency of measurement; and

b) The increase (decline) in earnings or economic value (or relevant measure used by management) for upward and downward rate shocks according to internal measurement of interest rate risk in the banking book.

Part IX. Enforcement

A. Sanctions for non-reporting of CAR breaches

1. It is the responsibility of the bank CEO to cause the immediate reporting of CAR breaches both to its Board and to the BSP. It is likewise the CEO's responsibility to ensure the accuracy of CAR calculations and the integrity of the associated monitoring and reporting system. Any willful violation of the above will be considered as a serious offense for purposes of determining the appropriate monetary penalty that will be imposed on the CEO. In addition, the CEO shall be subject to the following non-monetary sanctions:

a) First offense – warning;
b) Second offense – reprimand;
c) Third offense – 1 month suspension without pay; and
d) Further offense – disqualification.

B. Sanctions for non-compliance with required disclosures

2. Willful non-disclosure or erroneous disclosure of any item required to be disclosed under this framework in either the Annual Report or the Published Statement of Condition shall be considered as a serious offense for purposes of determining the appropriate monetary penalty that will be imposed on the bank. In addition, the CEO and the Board shall be subject to the following non-monetary sanctions:

a) First offense – warning on CEO and the Board;

b) Second offense – reprimand on CEO and the Board;

c) Third offense – 1 month suspension of CEO without pay; and

d) Further offense – possible disqualification of the CEO and/or the Board.

(Circular No. 538 dated 04 August 2006, as amended by Circular Nos. 605 dated 05 March 2008, 588 dated 11 December 2007, M-2007-019 dated 21 June 2007, Circular No. 560 dated 31 January 2007 and M-2006-022 dated 24 November 2006)

GUIDELINES ON THE CAPITAL TREATMENT OF BANKS' HOLDINGS OF REPUBLIC OF THE PHILIPPINES GLOBAL BONDS PAIRED WITH WARRANTS

[Appendix to Sec. 4115Q (2008 - 4116Q) and 4116Q]

A QB's holdings of ROP Global Bonds that are paired with Warrants (paired Bonds), which give the QB the option or right to exchange its holdings of ROP Global Bonds into Peso-denominated government securities upon occurrence of a predetermined credit event, shall be risk weighted at zero percent (0%): *Provided*, That the zero percent (0%) risk weight shall be applied only to QB's holdings of paired Bonds equivalent to not more than fifty percent (50%) of the total qualifying capital, as defined under *Appendix Q-46*.

(Circular 588 dated 11 December 2007)

GUIDELINES ON THE USE OF THE STANDARDIZED APPROACH IN COMPUTING THE CAPITAL CHARGE FOR OPERATIONAL RISKS

[Appendix to Sec. 4115Q (2008 - 4116Q) and 4116Q]

QBs applying for the use of the Standardized Approach (TSA) must satisfy the following requirements/ criteria:

General Criteria

1. The use of TSA shall be conditional upon the explicit prior approval of the BSP.

2. The BSP will only give approval to an applicant QB if at a minimum:

a. Its board of directors and senior management are actively involved in the oversight of the operational risk management framework;

b. It has an operational risk management system that is conceptually sound and is implemented with integrity; and,

c. It has sufficient resources in the use of the approach in the major business lines as well as in the control and audit areas.

3. The above criteria should be supported by a written documentation of the board-approved operational risk management framework of the QB which should cover the following:

a. Overall objectives and policies

b. Strategies and processes

c. Operational risk management structure and organization

d. Scope and nature of risk reporting/ assessment systems

e. Policies and procedure for mitigating operational risk

4. This operational risk management framework of the QB should be disclosed in its annual report, as provided under *Appendix Q-46*.

Mapping of Gross Income

5. QBs using TSA in computing operational risk capital charge must develop specific written policies and criteria for mapping gross income of their current business lines into the standard business lines prescribed under *Appendix Q-46*. They must also put in place a review process to adjust these policies and criteria for new or changing business activities or products as appropriate.

6. QBs must adopt the following principles for mapping their business activities to the appropriate business lines:

(a) Activities or products must be mapped into only one (1) of the eight (8) standard business lines, as follows:

(1) *Corporate finance*- This includes arrangements and facilities [e.g., mergers and acquisitions, underwriting, privatizations, securitization, research, debt (government, high yield), equity, syndications, Initial Public Offering (IPO), secondary private placements] provided to large commercial enterprises, multinational companies, NBFIs, government departments, etc.

(2) *Trading and sales*- This includes treasury operations, buying and selling of securities, currencies and others for proprietary and client account.

(3) *Retail banking*- This includes financing arrangements for private individuals, retail clients and small businesses such as personal loans, credit cards, auto loans, etc. as well as other facilities such as trust and estates and investment advice.

(4) *Commercial banking*- This includes financing arrangements for commercial enterprises, including project finance, real

estate, export finance, trade finance, factoring, leasing, guarantees, bills of exchange, etc.

(5) *Payment and settlement* - This includes activities relating to payments and collections, inter-bank funds transfer, clearing and settlement.

(6) *Agency services* - This refers to activities of QBs acting as issuing and paying agents for corporate clients, providing custodial services, etc.

(7) *Asset management* - This includes managing funds of clients on a pooled, segregated, retail, institutional, open or closed basis under a mandate.

(8) *Retail brokerage* - This includes brokering services provided to customers that are retail investors rather than institutional investors.

(a) Any activity or product which cannot be readily mapped into one (1) of the standardized business lines but which is ancillary[1] to a business line shall be allocated to the business line to which it is ancillary. If the activity is ancillary to two (2) or more business lines, an objective criteria or qualification must be made to allocate the annual gross income derived from that activity to the relevant business lines.

(b) Any activity that cannot be mapped into a particular business line and is not an ancillary[1] activity to a business line shall be mapped into one (1) of the business lines with the highest associated beta factor eighteen percent (18%). Any ancillary activity to that activity will follow the same business line treatment.

(c) QBs may use internal pricing methods to allocate gross income between business lines: *Provided*, That the sum of gross income for the eight business lines must still be equal to the gross income as would be recorded if the QB uses the Basic Indicator Approach (BIA).

(d) The process by which QBs map their business activities into the standardized business lines must be regularly reviewed by party independent from that process.

7. In computing the gross income of the QB, the amounts of the income accounts reported in the operational risk template[2] must be equal to the year-end balance reported in the FRP. Any discrepancy must be properly accounted and supported by a reconciliation statement.

Application Process for the Use of TSA

8. QBs applying for the use of TSA should submit the following documents to their respective Central Points of Contact (CPCs) of the BSP:

(a) An application letter signed by the president/CEO of the QB signifying its intention to use TSA in computing the capital charge for operational risk;

(b) Written documentation of the Board-approved operational risk management framework as described in paragraph 3.

(c) Written policies and criteria for mapping business activities and their corresponding gross income into the standard business lines as described in paragraphs 5 to 7.

(d) An overall roll-out plan of the QB including project plans and execution processes, with the appropriate time lines.

Initial Monitoring Period

9. The BSP may require a six (6)-month period of initial monitoring of a QB's TSA before it is used for supervisory capital purposes.

Reversion from TSA to BIA

10. A QB which has been approved to use TSA in computing its capital charge

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[1] Ancillary function is an activity/function that is not the main activity of a given business line but only as a support activity

[2] Part V of the revised CAR report template

for operational risk will not be allowed to revert to the simpler approach, i.e., the BIA. However, if the BSP determines that the QB no longer meets the qualifying criteria for TSA, it may require the QB to revert to BIA. The QB shall be required to repeat the whole application process should it opt to return to the use of TSA, but only after a year of using the BIA.

These guidelines shall take effect on 21 July 2007.

(M-2007-019 dated 21 June 2007)

GUIDELINES FOR TRUST DEPARTMENTS' PLACEMENTS IN THE SPECIAL DEPOSIT ACCOUNT FACILITY OF THE BANGKO SENTRAL

(Appendix to Subsec. 4409Q.2)

The following are the guidelines governing the trust deparments' placements in the SDA facility of BSP.

1. Access to the subject BSP facility shall be granted upon receipt by the BSP Treasury Department (BSP-TD) of a letter of request (*Appendix 78 Annex 1*) for account opening together with the following requirements:

a. Internal approvals allowing the trust department to invest in the BSP SDA facility;

b. A list of authorized signatories;

c. A list of authorized traders; and

d. Contact details for the front and back offices.

2. The trust department shall use a depository institution that is a PhilPASS member when placing its funds in the SDA facility. On transaction date, the trust department shall instruct said depository institution to debit their account in favor of their SDA with the BSP. Similarly, the trust department shall specify a PhilPASS member to which its principal and interest will be credited at maturity of the SDA placement.

3. Trading hours shall be from I0:00 am to 3:00 pm for all business days. All trades shall settle on trade date.

4. Applicable tenors and pricing shall be based on published rates (i.e., in Bloomberg's CBPHI and Reuters BANGKO page).

5. The existing tiering scheme, as detailed below shall be applied to the SDA placements of the trust departments separately from the placements of their bank proper.

Tier	Tiered Rate
Amounts less than or equal to P5.0 billion	BSP published rate
Amounts in excess of ₱5.0 billion up to ₱I0.0 billion	BSP published rate less 2%
Amounts in excess of ₱I0.0 billion	BSP published rate less 4%

6. The minimum placement is ₱10.0 million with the additional amounts in increments of ₱I .0 million.

7. Trust departments may place only once per tenor per day

8. Trust departments may pre-terminate their SDA placements, either fully or partially. If the holding period of the SDA placement when it is rate pre-terminated is less than fifty percent (50%) of the original tenor of the said placement, the applicable interest rate for the pre-terminated amount will be the rate dealt on value date less two percent (2%) p.a. If the holding period is fifty percent (50%) or more of the original tenor, the applicable interest rate for the pre-terminated amount will be the rate dealt on value date less one percent (1%) p.a. The pre-termination rate shall apply only to the amount pre-terminated.

9. The income from the SDA is subject to a twenty percent (20%) final withholding tax

10. Depository institution shall generally follow the existing settlement process for SDA placements with BSP of QBs. The trust department will be required to send the transaction confirmation directly to the BSP-TD back office. A sample confirmation is attached as *Appendix Q-47 Annex 1* and *Annex 2*.

11. Trust departments may request a statement from the BSP-TD for their outstanding SDA placement as of a specified date.

(*M-2007-011 dated 08 May 2007*)

Annex 1

(Institution's Letterhead)

Date:_____

Mrs. Ma. Ramona GDT Santiago
Managing Director
Treasury Department
Bangko Sentral ng Pilipinas

Dear Madam:

Pursuant to Monetary Board Resolution Nos. 433 and 518 dated 19 April 2007 and 03 May 2007, allowing trust departments to place their funds in the BSP's Special Deposit Account (SDA) facility, the trust department of (name of institution) respectfully request the creation of an account for the said facility.

Please find attached the following documents, as required:

a. Internal approvals allowing the trust department to invest in the SDA facility;
b. A list of authorized signatories;
c. A list of authorized traders; and
d. Contract details for the front and back offices.

For your kind attention.

Very truly yours,

_____
(AUTHORIZED SIGNATORY)1

_____
(AUTHORIZED SIGNATORY)2

Annex 2

(Institution's Letterhead)

Date:_____

TREASURY DEPARTMENT
Treasury Services Group - Domestic
Bangko Sentral ng Pilipinas

Gentlemen:

This is to confirm our **Special Deposit Account** placement to yourselves as follows:

VALUE DATE	
TERM	
MATURITY DATE	
RATE	
PRINCIPAL AMOUNT	
GROSS INTEREST	
WITHHOLDING TAX	
NET MATURITY VALUE	

On value date, our funds will come from Regular Demand Deposit account of (name of depository QB).

Accordingly, please **CREDIT** the Regular Demand Deposit Account of (name of depository QB) on maturity date the amount of _____PESOS (P_____), representing full payment of the principal plus interest (net of applicable withholding tax) thereon.

Very truly yours,

_____
(AUTHORIZED SIGNATORY)1

_____
(AUTHORIZED SIGNATORY)2

SPECIAL DEPOSIT ACCOUNT PLACEMENTS OF TRUST DEPARTMENTS/ ENTITIES AS AGENT FOR TAX-EXEMPT INSTITUTIONS AND ACCOUNTS

(Appendix to Subsection 4409Q.2)

Section 1. Placement of tax-exempt accounts in the SDA facility should comply with existing minimum placement and incremental requirements for the SDA facility.

Sec. 2. On transaction date, the trust department/entity must inform the BSP the exact amount of the tax-exempt placement in the SDA and submit the following supporting documents:

a. Copy of the relevant ruling from the BIR, duly certified by the latter, affirming the exemption from taxes of the income earned by concerned TEIs or accounts from their investments;

b. Copy of the board resolution duly certified by the corporate secretary authorizing the placement (directly for managed funds or indirectly through designated trustee bank/FI in the case of managed trust funds) in the SDA facility;

c. Copy of the covering trust agreement; and

d. Certification from the trust department that such placements, for as long as these are outstanding, are owned by the specified TEIs and are accordingly exempt from said twenty percent (20%) final withholding tax (FWT). Shown in Annex 1.

Advance copies may be sent through facsimile (facsimile number 523-3348) or electronic mail of BSP-Treasury Back Office personnel (jsiguenza@bsp. gov. ph).

Absent the supporting documents by end of the business day, the tax-exempt placement will be cancelled.

Sec. 3. For outstanding tax-exempt SDA placements as of 01 November 2007, trust departments must submit the documents specified in *Item* "2" hereof on or before 04 December 2007 to avail of the exemption from withholding tax.

(M-2007-038 dated 29 November 2007)

Annex 1

(Trust Entity/Department's Letterhead)

Date:_____

Ms. Ma. Ramona GDT Santiago
Managing Director
Treasury Department
Bangko Sentral ng Pilipinas
A. Mabini corner P. Ocampo Sts.
Manila 1004

Dear Ms. Santiago:

This refers to the placement/s amounting to ***(Peso Amount)*** placed in the BSP's SDA facility at ***(SDA rate)*** % per annum for value ***(Value date)*** to mature on ***(Maturity date)***.

This is to certify that the above placement/s is/are transacted on behalf of the following Tax-Exempt Institutions (TEI) or tax-exempt funds and interest income thereon are exempt from the twenty percent (20%) final withholding tax based on the corresponding BIR rulings:

Tax Exempt Institutions	**Basis (BIR Ruling No. and date)**	**Amount**
1.		
2.		
3.		
(rows may be increased depending on number of placements)		
TOTAL		

This is to further certify that above placements will be owned by the specified TEIs/tax-exempt funds for as long as these placements are outstanding.

In the event that the BSP is assessed for deficiency final withholding tax on the above placements by the Bureau of Internal Revenue (BIR), (NBFI name) shall be liable for and pay such deficiency taxes and surcharges, and/or indemnify/reimburse the BSP for such deficiency taxes and surcharges that the latter may eventually pay to the BIR as a result thereof. Further, (NBFI name) hereby authorizes the BSP to automatically debit its regular demand deposit account with the BSP for payment or reimbursement of any such deficiency taxes and surcharges.

Sincerely yours,

_____
HEAD OF TRUST DEPARTMENT

SUBSCRIBED AND SWORN to before me this ____ day of_____ 2007 at _____, affiant exhibiting to me his Community Tax Certificate/Passport No. _____, issued at _____, on _____.

Notary Public

Doc. No. _____;
Page No. _____;
Book No. _____;
Series of 200___

BASIC STANDARDS IN THE ADMINISTRATION OF TRUST, OTHER FIDUCIARY AND INVESTMENT MANAGEMENT ACCOUNTS

(Appendix to Subsec. 4401Q)

I. Introduction

Trust and other fiduciary business and investment management activities have evolved with the changes in the financial market and advancement in technology. These innovations have allowed trust entities to expand the scope of trust products and services offered to customers, thus increasing their exposure to various risks. As trust entities grow more diverse, necessarily policies and procedures as well as risk management practices must keep pace. The basic standards would provide common processes for an efficient operation and administration of trust, other fiduciary and investment management activities across the trust industry.

II. Statement of policy

It is the policy of the BSP to provide adequate level of protection to investors who, under a fiduciary arrangement, engage the services or avail of products of trust entities which are required to observe prudence in the exercise of their fiduciary responsibility. Along this line, the BSP prescribes basic standards for the efficient administration and operation of trust and other fiduciary business and investment management activities.

III. Standards

The basic standards in the administration of trust, other fiduciary and investment management accounts are meant to address the significant areas of operations and provide minimum set of requirements and procedures:

A. Account acceptance and review processes

1. Pre-acceptance account review

This review must document that the trust entity (TE) can effectively administer the account. It shall be covered by a written policy which shall contain, among other things, the types of trust, other fiduciary and investment management accounts that are desirable and consistent with the TE's risk strategies and the specific conditions for accepting new accounts, and approved by the Trust Committee, or the Trust Officer, or subordinate officer of the trust department, authorized by the board of directors or its functional oversight equivalent, in the case of foreign QBs and institutions.

The review process entails the thorough and complete review of the client's/account's characteristics and investment profile, including the assets/ properties to be contributed/ delivered. Non-financial/non-traditional assets (i.e., real estate and the like) which are more likely to be illiquid shall be carefully reviewed prior to acceptance to ensure that the TE only accepts accounts which hold assets it may be able to properly manage.

Prior to the acceptance of a fiduciary account, the TE shall review the underlying instrument (trust agreement or contract) for potential conflicts of interest. If such conflict exists, the TE shall take appropriate action to address such condition before the account is accepted.

In cases where the TE is chosen as a successor trustee or investment manager, the TE shall perform a review and evaluation of all assets to be delivered to the TE to determine how these would serve the client's objectives, whether the TE can properly handle such assets and to assess any possible issue/problem which may arise with respect to such assets before acceptance of such assets and/or assumption of the trust, fiduciary or investment management relationship.

2. Establishment and post-acceptance review. Acceptance policies for new accounts shall, at a minimum, include the following processes and/or requirements:

(1) *Account opening process*. This process defines the TE's policies and procedures for client/account identification, consistent with the TE's "know your customer" (KYC) policy for compliance with anti-money laundering regulations; identification of the needs of the client; the objective(s) of the engagement; the vehicle to be used; and the account's investment parameters. The trust officer or other authorized personnel of the trust department shall conduct the account opening process for trust, fiduciary and investment management accounts. In the case of unit investment trust funds (UITFs), only authorized branch managers/officers as well as UIT marketing personnel, who have all successfully undergone the required certification/accreditation/licensing process, may perform said process for UITF clients. The account opening process shall at least involve the following:

a. Client profiling shall be performed for all UITF and regular trust, other fiduciary and investment management accounts (except court trusts) via a duly acknowledged Client Suitability Assessment (CSA), which aims to provide the TE with information leading to the prudent design of investment packages, suited to a particular client or investment account. The profiling process, to be documented through a CSA Form signed by the concerned parties[1], shall be undertaken on a per client basis, which shall emphasize the level of risk tolerance of the client.

- Client suitability assessment

The TE shall obtain adequate information from the client to determine the appropriateness of the fiduciary product/service to be provided and ensure the suitability of the investment product/portfolio/strategy to be recommended to each client. It shall provide prospective clients with client suitability questionnaire and require them to accomplish the same prior to the acceptance of the account and execution of a transaction.

For this purpose, the TE shall make an assessment of the client's level of financial sophistication and consider factors relevant to the creation and management of, or participation in, an investment portfolio, such as but not limited to, the specific needs and unique circumstances of the client and/or beneficiary/(ies), basic characteristics of the clients' investment and experience, financial constraints, risk tolerance, tax considerations and regulatory requirements.

The same client suitability assessment process shall be applied by the TE for directional accounts.

- Minimum information required for CSA:

i. Personal/Institutional data. Minimum personal/institutional information that are unique to a natural or juridical client, which shall also cover demographics and KYC information; the identity of beneficiaries, where applicable, and approximate portion of total assets administered/managed.

ii. Investment objective. A clear statement or definition of the client's investment goals/purposes to be achieved through a particular trust, fiduciary or investment product or service. The client may opt to open several accounts, each one with specific investment objectives separate and distinct from the other accounts.

iii. Investment experience. A list of various types of investment the prospective client is familiar with, acquired from actual/personal investment experience, or of similar investment circumstances.

[1] i.e., the client, the UIT accredited marketing personnel or the officer of the trust department conducting the client profiling. The CSA Form shall be acknowledged or confirmed by the trust officer or other officer of the trust department autorized by board of directors.

iv. Knowledge and financial situation. For complex transactions where the level of risk involved is greater, the TE must take into account the knowledge, experience and financial situation of the client or potential client to assess the level of investment sophistication. This may include the careful assessment whether the specific type of financial instrument/service/ portfolio/strategy is in line with the client's disclosed financial capacity.

Such assessment is necessary as there are significant risks involved on financial investments (e.g., derivatives), the type of transaction (e.g. sale of options), the characteristics of the order (e.g., size or price specifications) or the frequency of the trading.

v. Investment time frame and liquidity requirement. The TE is able to organize the portfolio in a manner that will provide for anticipated liquidity requirement through redemption of principal contribution or earnings.

vi. Risk tolerance. Allow the TE to classify clients in accordance with its own pre-set internal risk classification.

Based on the results of the CSA, classification of clients by the TE may include, but need not be limited to the following:

i. *Conservative*. Client wants an investment strategy where the primary goal is to prevent the loss of principal at all times, and where the client prefers investment grade and highly liquid assets, government securities, ROP bonds, deposits with local QBs/ branches of foreign QBs operating in the Philippines, and deposits with FIs in any foreign country: *Provided*, That said FI has at least an investment grade credit rating from a reputable international credit rating agency. For purposes of investing in a UITF, a client wants an investment strategy where the primary objective is to prevent the loss of principal at all times and where the fund is invested in deposits with local QBs/ branches of foreign QBs operating in the Philippines and with FIs in any foreign country: *Provided,* That said FIs has at least an investment grade credit rating from a reputable international credit rating agency.

ii. *Moderate*. Client wants a portfolio which may provide potential returns on investment that are higher than the regular traditional deposit products and client is aware that a higher return is accompanied by a higher level of risk. Client is willing to expose the funds to a certain level of risks in consideration for higher returns.

iii. *Aggressive*. Client wants a portfolio which may provide appreciation of capital over time and client is willing to accept higher risks involving volatility of returns and even possible loss of investment in return for potential higher long-term results.

- Investment policy statement

The TE shall have in place a method by which suitability of investment is determined based on the results of the CSA and formulated via an Investment Policy Statement (IPS). It shall communicate to prospective clients the results of the assessment, recommend the investment product/portfolio/strategy, and explain the reasons why, on the basis of the given information, its recommendation is to the best interest of the client as of a defined timeframe. The TE shall make a recommendation only after having reasonably determined that the proposed investment is suitable to the client's and/or beneficiary's financial situation, investment experience, and investment objectives.

The IPS is a clear reference frame for investment decisions and must be based on the investment objectives and risk tolerance of the client. It must include, at a minimum, a description of the following:

i. Investment objective;

ii. Investment strategy-indicating how assets will be allocated indicating the agreed portfolio mix;

iii. Investment performance review – indicating proposed market benchmarks, if any and the desired frequency of the performance review/reporting;

iv. Investment limits – identifies any limitation which the client may have for the portfolio such as investment restrictions (e.g., prohibited investments) and client's consent for taking losses.

For UITF, the IPS is equivalent to the investment objective of the fund specifically stated in the Declaration of Trust.

- Option of client to re- classification

Generally, the TE shall recommend the investment product/portfolio/strategy suitable to the client based on the results of the CSA. The TE may, however, provide a process for allowing clients to invest in investment products/ portfolio/strategy with a higher risk than those corresponding to the CSA profile results. A client who exercises the option to be re-classified outside the CSA process thereby waives some of the protection afforded by these guidelines. Such re-classification may be allowed subject to the observance of the following:

i. The client shall state in writing to the TE that -

- He does not agree with or accept the recommendation of the TE on the investment product/portfolio/strategy appropriate to the client's profile based on the results of the CSA;
- He would like to avail of the investment product/portfolio/strategy other than that which is consistent with the results of the CSA;
- He requests/intends to be re-classified, either generally or in respect to a particular investment/service/ transaction/ product; and
- He fully understands and is willing to take the risks incidental to the investment product/portfolio/strategy to be availed of.

ii. The TE shall issue a clear written warning to the client of the protections he may lose and conversely, of the risks that he is exposed to.

iii. The TE shall have taken all reasonable steps to ensure that the client meets all relevant requirements as provided for in the TE's written policies.

- Frequency of CSA and IPS

i. The CSA shall be performed and the IPS shall be formulated and executed prior to the opening of the account;

ii. The TE shall update the CSA and the IPS at least every three (3) years except in the following instances;

- Whenever updates are necessitated by the client, upon notice/advise to the TE, on account of a change in personal/financial circumstances or preferences, the TE shall adjust/modify its investment strategy/ portfolio and recommendation, subject to the conformity of the client;
- Whenever managed trust, other fiduciary, and investment management accounts express intention to invest in complex investment products such as financial derivatives, the TE shall ensure that the CSA and the IPS are updated at least annually. Otherwise, the TE shall not make new/additional investments in complex investment products.

iii. The TE shall ensure that periodic written notices given to clients reminding them of such updates are received/ acknowledged by clients or their authorized representatives;

iv. Updated CSA and IPS shall be acknowledged by the client;

v. The frequency of review shall be included as a provision in the written agreement; and

vi. The latest CSA and IPS will continue to be applied for any subsequent principal contributions to the account, until these are amended or updated by the client.

b. Identification of degree of discretion granted by client to the TE. This process involves the determination of the extent of discretion granted to the TE to manage the client's portfolio.

(1) Discretionary. The TE has authority or discretion to invest the funds/property of the client in accordance with the parameters set forth by the client. Such authority of the TE which obtained a composite Trust Rating of "4" in the latest BSP examination will not be subject to the investment limitations provided under Subsecs. 4409Q.2 and 4409Q.3 for trust and other fiduciary accounts and Subsecs. 4411Q.4 and 4411Q.5 for investment management accounts, respectively; and

(2) Non-discretionary. Investment activity of the TE is directed by the client or limited only to specific securities or properties and expressly stipulated in the agreement or upon written instruction of the client.

(3) Documentation. The trust, fiduciary or investment management relationship shall be formally established through a written legal document such as the trust or investment management agreement. The engagement documents shall clearly specify the extent of fiduciary assignments/ responsibilities of the TE and articulate the nature and limits of each party's status as trustor/principal or trustee/agent. Policies and procedures shall provide that trust or investment management agreements are signed by the trust officer or , subordinate officer of the trust department, or in the case of UITFs, branch managers/officers duly authorized by the board of directors.

The documentation process must also consider the following:

a. The Agreement must conform to the requirements provided under Subsec. 4409Q.1 for trust and other fiduciary accounts and Subsec. 4411Q.1 for investment management accounts. In addition, the Agreement shall contain the following provisions:

i. A description of the services to be provided;

ii. All charges relating to the services or instruments envisaged and how the charges are calculated;

iii. The obligations of the client with respect to the transactions envisaged, in particular his financial commitments towards the TE; and

iv. For engagements involving management of assets or properties, the degree of discretion granted to the trustee or agent must be clearly defined and stated in the agreement;

b. The Agreement shall be in plain language understandable by the client and/ or personnel of the TE responsible for explaining the contents of the agreement to the client.

c. For complex investment products such as financial derivatives instruments or those that use synthetic investment vehicles, the TE shall disclose to the client and require client's prior written conformity to the following:

i. Key features of investment services and financial instruments envisaged, according to the nature of such instruments and services;

ii. The type(s) of instruments and transactions envisaged;

iii. The obligations of the TE with respect to the transactions envisaged, in particular, its reporting and notice obligations to the clients; and

iv. An appropriate disclosure bringing to the client's attention the risks involved in the transactions envisaged.

d. In order to give a fair and adequate description of the investment service or financial instrument, the TE shall provide a clearly stated and easily understood Risk Disclosure Statement to its clients, which forms part of or attached to the trust, fiduciary or investment management agreement. The Risk Disclosure Statement shall contain, among other things, the following provisions:

i. Cautionary statement on the general risks of investing or associated with financial instruments, i.e., if the market is not good, an investor may not be able to get back his principal or original investment. Such statement must be given due prominence, and not to be concealed or masked in any way by the wording, design or format of the information provided;

ii. If the investment outlet is exposed to any major or specific risks, a description and explanation of such risks shall be clearly stated; and

iii. Advisory statement that for complex investment products, said instruments can be subject to sudden and sharp falls in value such that the client may lose its/his entire investment, and, whenever applicable, be obligated to provide extra funding in case it/he is required to pay more later.

Additional risk disclosures may be provided as appropriate.

The TE must ensure that the trust, fiduciary and investment management agreements and documents have been reviewed and found to be legally in order.

B. Account administration

It is the fundamental duty of a fiduciary to administer an account solely in the interest of clients. The duty of loyalty is a paramount importance and underlies the entire administration of trust, other fiduciary and investment management accounts. A successful administration will meet the needs of both clients and beneficiaries in a safe and productive manner.

Account administration basically involves three processes, namely; (1) periodic review of existing accounts, (2) credit process and (3) investment process.

(1) Periodic review of existing accounts

The board of directors and Trust Committee shall formulate and implement a policy to ensure that a comprehensive review of trust, fiduciary and investment management accounts (including collective investment schemes such as UITFs) shall be conducted. The periodic review of managed accounts shall be aligned with the provisions on the review and updating of the CSA and IPS. The board of directors may delegate the conduct of account review to the Trust Officer or Trust Department Committee created for that purpose. The policy shall likewise indicate the scope of the account review depending upon the nature and types of trust, fiduciary and investment management accounts managed.

A comprehensive accounts review, which shall entail an administrative as well as investments review, shall be performed on a periodic basis to ascertain that the account is being managed in accordance with the instrument creating the trust and other fiduciary relationship. The administrative review of an account is taken to determine whether the portfolio/ assets are appropriate, individually and collectively, for the account, while an investment review is used to analyze the investment performance of an account and reaffirm or modify the pertinent investment policy statement, including asset allocation guidelines. Whether the administrative and investment review are performed separately or simultaneously, the reviewing authority shall be able to determine if certain portfolio/assets are no longer appropriate for the account, (i.e., not consistent with the requirements of the client) and to take proper action through prudent investment practices to change the structure or composition of the assets.

The periodic review process also involves disclosure of information on the investment portfolio and the relevant investing activities. Regardless of the degree of discretion granted by the client to the TE, the former assumes full risk on the investment and related activities, and counterparties. Relevant changes in the

TE's organization or investment policies that may affect the client's decision to continue the services of the TE shall be disclosed to the client.

In the case of non-discretionary public interest accounts such as employee benefit/retirement or pension funds, due diligence review of the investment portfolio by the TE shall include providing investors with appropriate information needed to make an informed investment decision and avoid possible conflict of interest and self-dealing situations.

The TE should be able to show (in addition to the specific written directive from the client) what it has done in the exercise of due diligence and prudence on its part to protect the interest of the client and/or beneficiaries, especially for accounts of public interest like retirement/pension fund accounts.

The TE shall keep its clients informed of the investment and related activities by rendering periodic reports and financial statements prescribed under Subsec. 4425Q.1 and as necessary. The types of reports and statements and the frequency of their submission must be clearly specified in the TE's written policies and procedures.

The TE shall also establish a system that enables a trust account representative or officer to periodically contact clients and/or beneficiaries to determine whether their financial objectives and circumstances have changed.

(2) Credit process

Each trust entity shall define its credit process in relation to the discharge of the TE's investment function. The process ensures credit worthiness of investment undertakings including dealings and relationship with counterparties. It also serves to institutionalize the independence of the credit process of the TE. The credit process must at least cover the following:

a. Credit policies. Trust entities must clearly define its credit policies and processes, including the use of internal and external credit rating and approval process relative to the delivery of its investment function. The TE can share credit information with the non-bank proper subject to proper delineation and documentation. The credit process shall show the following at the minimum:

i. Clear credit process flow, from initiation of the lending activities envisioned by the TE up to the execution of actual investment;

ii. Credit criteria and rating used;

iii. Manner by which the TE handles the information, including confidential and material data, which is shared between and among the departments, subsidiaries or affiliates of the TE; and

iv. Clear delineation of duties and responsibilities of each of the departments, subsidiaries and affiliates of the TE, where such groups or entities share the credit process.

b. Counterparty accreditation process The TE must clearly define the policies and the processes it will undertake to accredit counterparties, including the non-bank proper, and its subsidiaries and affiliates, for their investment trading functions. It may use or avail itself of the accreditation process of its non-bank proper, provided there is proper delineation of functions. The counterparty accreditation process shall show the following at the minimum:

i. Clear accreditation process flow from the initiation of credit activities up to the actual usage of lines;

ii. Credit criteria and rating used;

iii. Manner by which the TE handles the information, including confidential and material data, which are shared between and among the departments, subsidiaries or affiliates of the TE;

iv. Usage, duties and responsibilities of each of the department, subsidiaries and affiliates of the TE, where there is sharing of credit lines between and among these concerned groups/ entities; and

v. Clear delineation of duties and responsibilities of each of the departments, subsidiaries and affiliates of the TE, where such groups or entities share the accreditation credit process.

(3) Investment process

This process defines the investment policies and procedures, including decision-making processes, undertaken by the TE in the execution of its fund/asset management function. The primary objective of such process is to create a structure that will assure TEs observe prudence in investment activities at all levels, preservation of capital, diversification, a reasonable level of risk as well as undivided loyalty to each client and adherence to established structure for the TE's investment undertakings. The investment process covers a broad range of activities; thus, the investment policies shall clearly outline the parameters that, at a minimum, include the following:

a. Overall investment philosophy, standards and practices. A general statement of principles that guides the portfolio manager in the management of investments outlined in the board-approved policy, along with a discussion on the practices and standards to be implemented to achieve the desired result.

b. Investment policies and processes. Defines the policies and the processes undertaken to create the portfolio to ensure the proper understanding of the client's preferences.

i. Profiling of client. Aims to understand the level of maturity of the client relevant to the creation of an appropriate portfolio.

ii. Portfolio construction for custom-made portfolios. Includes the process of researching and selecting recommended portfolio and setting objectives or strategies for diversification by types and classes of securities into general and specialized portfolios.

- Asset allocation. Outlines the process and criteria for selecting and evaluating different asset classes identified to be appropriate for the client's profile and investment objective. It includes the allocation of desired tenors in conjunction with the client or portfolio profile based on the CSA or IPS. The asset allocation may be based on percentage to total funds managed by the TE or stated in absolute amount whichever is preferred by the client.
- Security selection. Policies and procedures on the selection of investment outlets, including investment advisory, must be in place. This involves the selection of issuers for each of the identified asset classes. The process provides for the review of investment performance using risk parameters and comparison to appropriate benchmarks. It shall also identify the documentation required for all investment decisions.

If the TE uses approved lists of investments, there shall be an outline of the criteria for the selection and monitoring of such investments, as well as a description of the overall process for addition to and deletion from the lists.

- Benchmark selection/creation Selects or crafts the benchmarks to reflect the desired return of the portfolio and to measure the performance of the portfolio manager. The TE shall be required to measure performance based on benchmarks to gauge or measure the performance of the account. The TE must have clear definition of its benchmarking policy.
- Limits. Identifies any limitations on portfolio management which the client may impose on the TE. These limitations have to be specific as to the nature of the portfolio, such as but not limited to, core holdings, investment in competitor companies, and companies engaged in vices.
- Risk disclosure statement. A clear and appropriately worded statement/s to

disclose different risks to clients of the various investment undertakings of the investment manager done in behalf of the client.

iii. Internal policies on trade allocation. Defines the institution's policies in ensuring timely, fair and equitable allocation of investments across investing portfolios.

iv. Diversification of discretionary investments. The TE shall have a policy on the general diversification requirements for asset administration, as well as the process implemented to monitor and control deviations from policy guidelines.

v. A TE shall have access to timely and competent economic analyses and forecasts for the capital markets and other products in which its clients will be investing. TEs engaged in more complex transactions may consider providing an economic and securities research unit that continually monitors global trends and capital markets. This unit provides necessary forecasts of capital market expectations, currency relationships, interest rate movements, commodity prices, and expected returns of asset classes and individual investment instruments, which help the TE establish appropriate investment policies and strategies, select appropriate investments, and manage risks effectively.

vi. The TE shall have a process that will confirm trust personnel with investment functions know and follow the BOD-approved investment policies and processes.

c. Selection and use of brokers/ dealers. The quality of execution is an important determinant in broker selection. In selecting brokers/dealers, a TE must consider the following minimum standards and criteria:

i. Execution capability and ability to handle specialized transactions;

ii. Commission rates and other compensation;

iii. Financial strength, including operating results and adequacy of capital and liquidity;

iv. Past record of good and timely delivery and payment on trades;

v. Value of services provided, including research; and

vi. Available information about the broker from other broker customers, regulators, and self-regulated organizations authorized by the SEC.

The TE with large portfolio may opt to evaluate broker performance using a formalized point scoring system. A list of approved brokers shall be made available by the TE, reviewed periodically and updated at least annually.

d. Best practices. The TE shall document best practices policies and processes to institutionalize proper safeguards for the protection of its clients and itself. At a minimum, the policies must include the following standards:

i. Best execution. The TE shall use reasonable diligence to ensure that investment trades are executed in a timely manner and on the best available terms that are favorable to the client under prevailing market conditions as can be reasonably obtained elsewhere with an acceptable counterparty. For related counterparties, no purchase/sale must be made for discretionary accounts without considering at least two (2) competitive quotes from other sources. The policy on best execution must document processes to warrant such execution is readily and operationally verifiable.

ii. Chinese wall. A clear policy on Chinese wall aims to protect the institution from conflict of interest arising from varying functions carried by the TE in relation to credit (debt), shareholder, and investment position taking. The policy shall state the duties and responsibilities of the TE and each department including that of the non-bank proper and subsidiaries and

affiliates should transactions involve the concerned departments and entities.

iii. Personnel investment policies These policies aim to ensure honest and fair discharge of investment trading functions of all qualified personnel. Qualified personnel are those that may have access to information on clients and investment position-taking of clients, investment manager or portfolios. The use of such information may be abused and detrimental to the clients. The policy shall state the duties and responsibilities of each qualified personnel in relation to trading and portfolio management activities including allowed and not allowed transactions as well as sanctions in case of violations.

iv. Confidentiality and materiality of information. The TE must keep information about past, current and prospective clients confidential, unless disclosure is authorized in writing by the client or required by law and the information involve illegal activities perpetrated by the client. It must ensure safekeeping of confidential and material information and prevent the abuse of such information to the detriment of the institution or its clients.

v. Fair dealing. The TE shall document dealing practices to ensure fair, honest and professional practices in accordance with the best interest of the client and counterparties at all times and for the integrity of the market. It must ensure that any representations or other communications made and information provided to the client are accurate and not misleading. The TE must also take care not to discriminate against any client but treat all clients in a fair and impartial manner.

vi. Diligence and reasonable basis. In conducting its investment services, the TE shall act with skill, and care and diligence, and in the best interests of its clients and the integrity of the market. The duty of due diligence is intertwined with the duty to maintain independence and objectivity in providing investment recommendations or taking investment actions. When providing advice to a client, the TE shall act diligently and make certain that its advice and recommendations to clients are based on thorough analysis and take into account available alternatives.

- The TE shall take all reasonable steps to execute promptly client orders in accordance with the instruction of clients.
- The TE, when acting for or with clients, shall always execute client orders on the best available terms.
- The TE shall ensure that transactions executed on behalf of clients are promptly and fairly allocated to the accounts of the clients on whose behalf the transactions were executed.

Where a client opts not to accept the recommendation of the TE and chooses to purchase another investment product which is not recommended, the TE may proceed with the client's request/ instruction, provided it shall document the decision of the client and highlight to him/ her that it is his/her responsibility to ensure the suitability of the product selected.

vii. In-House or related party transactions handling. The TE shall define the policies in handling related-interest transaction to ensure that the best interest of clients prevails at all times and all dealings are above board. It must conform to the requirements of Subsecs. 4409Q.3 and 4411Q.5.

viii. Valuation. The TE shall document the institution's valuation process to show the sources of prices, either market or historical value, and the formula used to derive the NAV of investment portfolios. Valuation shall be understood, compliant with written policies and operating procedures, and used consistently within the TE. The TE must ensure that the valuation processes of service providers, custodians, and other subcontractors are compatible with those of the TE and in compliance with relevant statutory or regulatory valuation standards.

Risk officers shall document the accuracy and reliability of all valuation processes and data sources and ensure that valuations are completed as required by internal policies and procedures and regulatory reporting standards.

e. Conflicts of interests. These may arise when the TE exercises any discretion where mutually opposing interests are involved. The most serious conflict of interest is self-dealing, which could include transactions such as an investment in related interests of the TE or purchase of securities from or through an affiliate. Such transactions must be fully disclosed and authorized in writing by clients. Because of the complexity and sensitivity of the issue, a TE must develop policies and procedures to identify and deal with conflicts of interest situations.

3. Account termination

Accounts may be terminated for a variety of reasons, including the occurrence of a specified event or upon written notice of either the client or the TE. The trust or investment management agreement shall provide for the terms and manner of liquidation, return and delivery of assets/ portfolio to the client. Generally, the TE's responsibilities include distribution to the client, the successor trustee and/or beneficiaries of the remaining assets held under trusteeship/agency arrangement, preparation and filing of required reports. The TE must ensure that risk control processes are observed when terminating accounts just as when accepting them.

The TE must have a general policy with respect to the termination of trust accounts, which policy shall take into consideration the general processes to be observed in the return or delivery of different types of assets, the possible modes of distribution, fees to be paid, taxes to be imposed, the documentation required to effect the transfer of assets, the provision of terminal reports, and whenever applicable, the timing of distribution, needs and circumstances of the beneficiaries. Should the TE anticipate possible issues or problems with respect to the termination of the account, such as the liquidation of certain assets or the partition or division of assets, these issues shall be disclosed to the client for proper disposition. The policy on the termination of trust, fiduciary and investment management accounts shall likewise include the approval process to be observed for the termination of these accounts as well as the reporting requirements for accounts terminated and closed.

(Circular No. 618 dated 20 August 2008)

GUIDELINES FOR DAYS DECLARED AS PUBLIC SECTOR HOLIDAYS

[Appendix to 4256Q and 4601Q.6 (2008 - 4246Q.2 and 4601Q.6)]

Time of receipt of Public Holiday Announcement by the BSP	Bangko Sentral ng Pilipinas							Reserve Position	Bureau of the Treasury		PCHC	
	Treasury Department				PDS	PhilPASS	Cash Dept Withdrawal		Auction	Sec. Mkt.	Manila	Regional
	Overnight RP/RRP		Term RP& RRP/GS/ SDA/RDA									
	Trading	Settlement	Trading	Settlement								
1. On an ordinary business day prior to the date of effectivity	Closed	Closed	Closed	Closed	Closed	Closed	Closed	Non-Reserve	Closed	Closed	No clearing; no settlement. PCHC will issue an advisory to its members that it will continue accepting and processing checks	To be decided in coordination with Head Office
2. On a Saturday or Sunday to take effect the following Monday or on a non-working holiday to take effect the next business day												
a. Under good weather condition	No change in trading hours	No change in settlement time	No change in trading hours	No change in settlement time	Open	Open	Open	Reserve	Open	Open	Normal	To be decided in coordination with Head Office
b. Under unfavorable conditions such as bad weather, (e.g. Typhoon signal no. 3), natural calamities or civil disturbances	Closed	Closed	Closed	Closed	Closed	Closed	Closed	Non-Reserve	Closed	Closed	No clearing; no settlement. PCHC will issue an advisory to its members that it will continue accepting and processing checks	To be decided in coordination with Head Office

Time of receipt of Public Holiday Announcement by the BSP		Bangko Sentral ng Pilipinas							Reserve Position	Bureau of Treasury		PCHC	
		Treasury Department				PDS	PhilPASS	Cash Dept Withdrawal		Auction	Sec. Mkt.	Manila	Regional
		Overnight RP/RRP		Term RP& RRP/GS/ SDA/RDA									
		Trading	Settlement	Trading	Settlement								
3. Before 9:00 a.m. on the date of effectivity		Closed	Closed	Closed	Closed	Closed	Closed	Closed	Non-Reserve	Closed	Closed	No clearing; no settlement. PCHC will issue an advisory to its members that it will continue accepting and processing checks	To be decided in coordination with Head Office
4. After 9:00 a.m. on the date of effectivity	Day 1	Suspended to be resumed the following day at 9:01a.m. to 9:45 a.m.		No change in trading hours	No change in settlement time	Open	Open	Open	Reserve	Open	Open	Normal	To be decided in coordination with Head Office
	Day 2	Resumed from 9:01 a.m. to 9:45 am (for value Day 1) then, 4:45p.m. to 5:30p.m. for same day transaction	9:01 a.m. to 10:00 a.m. 4:45p.m. to 5:45p.m.	No change in trading hours	No change in settlement time	Open	Open	Open	Reserve	Open	Open	Normal	To be decided in coordination with Head Office
5. In case of suspension of work is extended to Day 2													
a. Before 9:00am of Day 2	Day 2	closed; Day 1 transactions will be moved to Day 3 (for value Day 1)	Closed	Closed	Closed	Closed	Closed	Closed	Non-Reserve	Closed	Closed	No clearing; no settlement PCHC will issue an advisory to its members that it will continue accepting and processing checks	To be decided in coordination with Head Office

Time of receipt of Public Holiday Announcement by the BSP		Bangko Sentral ng Pilipinas							Reserve Position	Bureau of Treasury		PCHC	
		Treasury Department				PDS	PhilPASS	Cash Dept Withdrawal					
		Overnight RP/RRP		Term RP& RRP/GS/ SDA/RDA						Auction	Sec. Mkt.	Manila	Regional
		Trading	Settlement	Trading	Settlement								
	Day 3	Resumed from 9:01 a.m. to 9:45 am (for value Day 1) then, 4:45p.m. to 5:30p.m. for same day transaction	9:01 a.m. to 10:00 am 4:45p.m. to 5:45p.m.	No change in trading hours	No change in settle-ment time	Open	Open	Open	Reserve	Open	Open	Normal	To be decided in coordination with Head Office
b. After 9:00 a.m. of Day 2	Day 2	Resumed from 9:01 a.m. to 9: 45 a.m. (for value Day 1) then, Day 2 transactions suspended to be resumed the following day from 9:01a.m. to 9:45 a.m.	9:01 a.m. to 10:00 a.m. 4:45p.m. to 5:45p.m.	No change in trading hours	No change in settlement time	Open	Open	Open	Reserve	Open	Open	Normal	To be decided in coordination with Head Office

Time of receipt of Public Holiday Announcement by the BSP		Bangko Sentral ng Pilipinas							Reserve Position	Bureau of Treasury		PCHC	
		Treasury Department				PDS	PhilPASS	Cash Dept Withdrawal		Auction	Sec. Mkt.	Manila	Regional
		Overnight RP/RRP		Term RP& RRP/GS/ SDA/RDA									
		Trading	Settlement	Trading	Settlement								
	Day 3	Resumed from 9:01 a.m. to 9:45 am (for value Day 2) then, 4:45p.m. to 5:30p.m. for same day transaction	9:01 a.m. to 10:00 a.m. 4:45p.m. to 5:45p.m.	No change in trading hours	No change in settlement time	Open	Open	Open	Reserve	Open	Open	Normal	To be decided in coordination with Head Office
6. In case the suspension of work does not apply to all government offices (Manila Day, Quezon City Day, etc.)		4:45 p.m. to 5:30 p.m. for same day transaction	4:45 p.m. to 5:45 p.m.	No change in trading hours	No change in settlement time	Open	Open	Open	Reserve	Open	Open	Normal	To be decided in coordination with Head Office

(M-2008-025 dated 13 August 2008)

GUIDELINES ON THE SUBMISSION OF APPLICATION FOR MERGER AND CONSOLIDATION

(Appendix to Subsec. 4108Q.1)

The following guidelines and procedures shall be observed by non-bank financial institutions with quasi-banking functions (NBQBs) in their application for merger/consolidation:

1. The merging/consolidating entities shall comply with the safety and soundness test requirements as follows:

a. Compliance, especially by the acquiring NBQB, with major banking laws and regulations; and

b. Submission to the BSP of a satisfactory action plan, if applicable, to address serious supervisory concerns.

2. Submission of the following documentary requirements simultaneously to the BSP and the PDIC for merger/ consolidation application involving only NBQBs;

a. Articles of Merger or Consolidation duly signed by the President or Vice-President and certified by the secretary or assistant secretary of each of the constituent institutions setting forth the following as required in Section 78 of the Corporation Code:

- The Plan of Merger or Consolidation;
- The number of shares outstanding; and
- The number of shares voting for and against the Plan, respectively.

b. Plan of Merger or Consolidation setting forth the following:

- The names of the constituent institutions;
- The terms of the merger or consolidation and the mode of carrying the same into effect;
- A statement of the changes, if any, in the Articles of Incorporation of the surviving institution in the case of merger; and in the case
- Of consolidation, all the statements required to be set forth in the Articles of Incorporation;
- Such other provisions with respect to the proposed merger or consolidation as are deemed necessary or desirable.

c. Resolution of the Board of Directors of the respective institutions approving the Plan of Merger or Consolidation. The resolution shall be certified under oath by the respective corporate secretaries of the constituent institutions;

d. Resolution of the meeting of the stockholders in which at least two-thirds (2/3) of the outstanding capital stock of each corporation have approved the plan of merger or consolidation. The resolution shall be certified under oath by the respective corporate secretaries of the constituent institutions;

e. Financial Statements:

- Latest financial statements and three (3) - year audited financial statements of the merging institutions
- Three (3) - year financial projections with valid assumptions of the merged or consolidated institutions' balance sheet and income statement.

f. List of merger incentives the bank will avail of;

g. List of stockholdings of each of the constituent institutions before and after the merger;

h. List of directors and officers of each of the merging/consolidating institutions;

i. List of proposed officers and directors of the merged or consolidated institution and the summary of their qualifications;

j. Organizational chart of the merged or consolidated institution including the number of offices and locations thereof;

k. Inter-company transactions relative to the submitted Financial Statements;

l. Computation of Capital Adequacy Ratio on the submitted financial Statements;

m. Viable Operational Plan with the following components:

- Marketing Strategies
- Proposed Loan Portfolio Diversification
- Deposit Generation
- Proposed Improvements in Accounting System
- Operational Control
- Computerization Plan
- Communication System

n. The appraiser's report of reappraisal of NBQB premises, if any, done by an independent and licensed appraiser;

o. Proposed increase of capital stock of surviving NBQB;

p. Proposed amendments in the Articles of Incorporation of surviving NBQB;

q. Director's Certificate (surviving NBQB) on the proposed amendment of the Articles of Incorporation increasing the authorized capital stock; and

r. Any other reasonable requirement deemed material in the proper evaluation of the merger or consolidation as may subsequently be requested by the BSP and/or PDIC.

3. For merger/consolidation involving a NBQB, the BSP shall wait for PDIC consent before elevating the proposed merger/consolidation to the Monetary Board for approval; and

4. The authority given to merge/consolidate the constituent entities shall be valid within six (6) months reckoned after BSP approval.

(M-2009-028 dated 12 August 2009)

GUIDELINES ON THE COLLECTION OF THE ANNUAL SUPERVISORY FEES FOR THE YEAR 2010

[Appendix to Subsec. 4901Q.1 (2008 - 4652Q)]

The following guidelines shall govern the collection by the BSP and the payment by QB of the 2010 Annual Supervisory Fees (ASF).

1. Notification of amount due for 2010 ASF and mode of payment. The BSP Supervisory Data Center (SDC) shall send a billing notice in June 2010 to the QB for its ASF payment indicating, among others, the computation of the ASF due, including the 2% creditable withholding tax (CWT) thereon, if applicable, the period covered by the ASF and the specific date when the ASF will be debited from the QB's demand deposit account (DDA) with the BSP.

The BSP will not accept checks as mode of ASF payment. QBs, upon receipt of the ASF billing notice from the BSP, should maintain adequate balance in their DDA to cover the ASF and other daily obligations and, when necessary, make corresponding deposits to fully cover said obligations. In case of deficiency, the provisions on DDA deficiency in Subsec. X4901Q.1, as amended, shall apply.

2. Exceptions noted on billing notice of 2010 ASF. Upon receipt of the BSP Notice of ASF billing, a QB is encouraged to check the accuracy of the billing and to submit any of the noted exceptions therein not later than ten (10) days before the specified date of collection/debit to DDA as indicated in the billing notice. The said exceptions, together with supporting documents, shall be submitted to:

The Director
Supervisory Data Center (SDC)
Bangko Sentral Ng Pilipinas
16th Floor, Multi-Storey Building
BSP Complex, A. Mabini Street
Malate, Manila 1004

Any exceptions received after the cut-off date or any exception not duly substantiated with documents before the cut-off date will be evaluated and considered in the computation of the ASF for the immediate succeeding year.

3. Withholding tax on 2010 supervisory fees. The following shall apply to QBs covered by Sections M and N of BIR Revenue Regulations (R.R.) No. 2-98, as amended by R.R. No. 17-2003:

a. Within tern (10) days from 31 May 2010, the QB shall submit to the BSP (at the address indicated in Item "2" hereof) a certified true copy of the BIR notice classifying it as among the institutions covered under Section M of R.R. No. 2-98, as amended by R.R. No. 17-2003. Such BIR notice received by the BSP after cut-off of ten (10) days will be considered in teh ASF computation of the next year. The submission of such BIR notice will no longer be necessary if previously transmitted and received by the BSP in compliance with Section 3.1 of the BSP Memorandum No. 2009-0046 dated dated 17 November 2009.

b. The ASF, net of the 2% CWT, shall be debited from the DDA on the specified date referred to in the notice of ASF billing under Item *"1"*.

c. The following timelines shall be observed on the submission of annual withholding tax documents to BSP at the address indicated in Item *"2"* hereof:

Tax Documents	Due Date
1. Original copy of BIR Form No. 2307 - Certificate of Creditable Tax Withheld at Source	On or before 31 December 2010

Tax Documents	Due Date
2. Original Duplicate Copy of BIR Form No. 1601E - Monthly Remittance Return of Creditable Income Taxes Withheld (Expanded), duly received by BIR, If manually filed, or duly supported with BIR confirmation notice/ advice, if elctronically filed	On or before 31 December 2010
3. Certified true copy of BIR official receipt/payment confirmation receipt	On or before 31 December 2010

d. Considering that the withholding tax documents enumerated in Item "c" will be used to avail the tax credits for filing the annual income tax return of the BSP, the failure to submit all of the enumerated documents within the stated deadline will compel the BSP to immediately debit an amount equivalent to the 2% CWT from the DDA of QBs concerned, with no obligation on the part of the BSP to reimburse said amount in case of late submission. In case of DDA deficiency, the provisions in Subsec. 4901Q.1, as amended, shall apply.

The above guidelines on withholding tax shall be strictly enforced pending resolution of the tax treatment on the ASF being assessed by the BSP.

(M-2009-004 dated 12 February 2009, as amended by M-2010-013 dated 31 May 2010 and M-2009-046 dated 17 November 2009)

GUIDELINES ON BANKS' INTERNAL CAPITAL ADEQUACY ASSESSMENT PROCESS

(Appendix to Sec. 4119Q)

A. Introduction

1. This document sets out the broad guidelines that UBs and KBs (hereinafter referred to as 'banks') should follow in the design and use of their Internal Capital Adequacy Assessment Process (ICAAP). A bank's ICAAP supplements the BSP's Risk-Based Capital Adequacy Framework (the Framework) as contained in existing regulations and, thus, must be applied on a group-wide basis, i.e., it should cover all of a bank's subsidiaries and affiliates.

2. Although the Framework prescribes the guidelines for determining banks' minimum regulatory capital requirements in relation to their exposure to credit risk, market risk and operational risk, a bank's Board of Directors and senior management are still ultimately responsible in ensuring that the bank maintains an appropriate level and quality of capital commensurate not just with the risks covered by the Framework, but also with all other material risks to which it is exposed. Hence, a bank must have in place an ICAAP that takes into account all of these risks.

B. Guiding principles

1. Banks must have a process for assessing their capital adequacy relative to their risk profile (an ICAAP).

2. The ICAAP is the responsibility of banks. Banks are responsible for setting internal capital targets that are consistent with their risk profile, operating environment, and strategic/business plans. The ICAAP should be tailored to a bank's circumstances and needs, and it should use the inputs and definitions that a bank normally uses for internal purposes.

3. Banks' ICAAP (i.e., the methodologies, assumptions and procedures) and other policies supporting it (e.g., capital policy, risk management policy, etc.) should be formally documented, and they should be reviewed and approved by the board. The results of the ICAAP should also be regularly reported to the board.

In addition, the board and senior management are responsible for integrating capital planning and capital management into banks' overall management culture and approach. They should ensure that formal capital planning and management policies and procedures are communicated and implemented group-wide and supported by sufficient authority and resources.

Banks' ICAAP document should be submitted to the appropriate Central Point of Contact Department (CPCD) of the BSP every 31 January of each year. A suggested format of the ICAAP submission to the BSP is provided in *Annex A* of *Appendix Q-52*.

4. The ICAAP should form an integral part of banks' risk management processes so as to enable the board and senior management to assess, on an on-going basis, the risks that are inherent in their activities and material to their bank. This could range from using the ICAAP in more general business decisions (e.g. expansion plans) and budgets, to the more specific decisions such as allocating capital to business units, or to having it play a role in the individual credit decision process.

5. The ICAAP should be reviewed by the board and senior management at least annually, or as often as is deemed necessary

to ensure that risks are covered adequately and that capital coverage reflects the actual risk profile of their bank. Moreover, any changes in a bank's strategic focus, business plan, operating environment or other factors that materially affect assumptions or methodologies used in the ICAAP should initiate appropriate adjustments to the ICAAP. New risks that occur in the business of a bank should be identified and incorporated into the ICAAP. The ICAAP and its review process should be subject to independent internal or external review. Results thereof should be communicated to the board and senior management.

6. Banks should set capital targets which are consistent with their risk profile, operating environment, and business plans. Banks, however, may take other considerations into account in deciding how much capital to hold, such as external rating goals, market reputation and strategic goals. If these other considerations are included in the process, banks must be able to show to the BSP how they influenced their decisions concerning the amount of capital to hold.

7. The ICAAP should capture the risks covered under the Framework – credit risk, market risk, and operational risk. If applicable, banks should disclose major differences between the treatments of these risks in the calculation of minimum regulatory capital requirement under the Framework and under the ICAAP. In addition, the ICAAP should also consider other material risks that banks are exposed to, albeit that there is no standard definition of materiality. Banks are free to use their own definition, albeit that they should be able to explain this in detail to the BSP, including the methods used, and the coverage of all material risks. These other material risks may include any of the following:

a. Risks *not fully* captured under the Framework, for example, credit concentration risk, risk posed by non-performing assets, risk posed by contingent exposures, etc.;

b. Risks *not* covered under the Framework. As a starting point, banks may choose to use the other risks identified under Circular No. 510 dated 03 February 2006. Some of these risks are less likely to lend themselves to quantitative approaches, in which cases banks are expected to employ more qualitative methods of assessment and mitigation. Banks should clearly establish for which risks a quantitative measure is warranted, and for which risks a qualitative measure is the correct risk assessment and mitigation tool; and

c. Risk factors external to banks. These include risks which may arise from the regulatory, economic or business environment.

8. Banks should have a documented process for assessing risks. This process may operate either at the level of the individual banks within the banking group, or at the banking group level. Banks are likely to find that some risks are easier to measure than others, depending on the availability of information. This implies that their ICAAP could be a mixture of detailed calculations and estimates. It is also important that banks not rely on quantitative methods alone to assess their capital adequacy, but include an element of qualitative assessment and management judgment of inputs and outputs. Non-quantifiable risks should be included if they are material, even if they can only be estimated. This requirement might be eased if banks can demonstrate that they have an appropriate policy for mitigating/managing these risks.

9. The ICAAP should take into account banks' strategic plans and how they

relate to macro-economic factors. Banks should develop an internal strategy for maintaining capital levels which can incorporate factors such as loan growth expectations, future sources and uses of funds and dividend policy, and any procyclical variation of minimum regulatory capital requirements.

Banks should also have an explicit, board-approved capital plan which states their objectives and the time horizon for achieving those objectives, and in broad terms the capital planning process and the responsibilities for that process. The plan should also lay out how banks will comply with capital requirements in the future, any relevant limits related to capital, and a general contingency plan for dealing with divergences and unexpected events (for example, raising additional capital, restricting business, or using risk mitigation techniques).

In addition, banks should conduct appropriate scenario/stress tests which take into account, for example, the risks specific to the particular stage of the business cycle. Banks should analyze the impact that new legislation/regulation, actions of competitors or other factors may have on their performance, in order to determine what changes in the environment they could sustain.

10. The results and findings of the ICAAP should feed into banks' evaluation of their strategy and risk appetite. For less sophisticated banks in particular, for which genuine strategic capital planning is likely to be more difficult, the results of the process should mainly influence the bank's management of its risk profile (for example, via changes to its lending behavior or through the use of risk mitigants). The ICAAP should produce a reasonable overall capital number and assessment. Banks should be able to explain to the BSP's satisfaction the similarities and differences between its ICAAP and its minimum regulatory capital requirements under the Framework.

C. ICAAP Methodologies

1. While banks may use simple or model-based ICAAP methodologies depending on what they think is appropriate for them *(please see Annex B of Appendix Q-52 for description of the different broad classification of methodologies),* at the minimum, the BSP expects banks to adopt an ICAAP based on the minimum regulatory capital requirement under the Framework and, where applicable, assess extra capital proportionate to the other risks that are not covered under said Framework. This requires an assessment first of whether the risks covered under the Framework - credit risk, market risk and operational risk - are fully captured, and second, how much capital to allocate against other risks and external factors.

2. Regardless of which methodology a bank decides to adopt, it should compare its actual and future projected capital with the actual and future internal capital need arising from the assessment. The actual calculation and allocation of capital always needs to be supplemented by sufficiently robust qualitative procedures, measures and provisions to identify, manage, control and monitor all risks.

3. The ICAAP will always consist of two parts. One part covers all steps necessary for assessing the risks. The other part covers all steps necessary to assess the actual capital (risk-taking capacity). As these two parts will always meet at the end of the ICAAP and have to be in balance, there is no procedure which says which part has to be assessed first.

4. After choosing its ICAAP methodology, a bank could take its thinking through the following steps in developing the ICAAP:

a. Risk identification

A bank could prepare a list of all material risks to which it is exposed; for that purpose it may find it useful to identify and consider its largest past losses and whether those losses are likely to recur. The identification of all material risk to which a bank is exposed should be conducted in a forward looking manner.

b. Capital assessment

For all the risks identified through the process above, a bank could then consider how it would act, and the amount of capital that would be absorbed, in the event that one or more of the risks identified was to materialize.

c. Forward capital planning

A bank could then consider how its capital need as calculated above might change in line with its business plans over its strategic time horizon, and how it might respond to these changes. In doing so, a bank may want to perform a sensitivity analysis to understand how sensitive its capital is to changes in internal and external factors such as business risks, and changes in economic/business cycles.

d. ICAAP outcome

Finally, a bank should document the ranges of capital required as identified above and form an overall view on the amount of internal capital which it should hold.

(Circular No. 639 dated 15 January 2009)

Annex A

INTERNAL CAPITAL ADEQUACY ASSESSMENT PROCESS
(Suggested Format)

The BSP expects that there will be a fair degree of variation in the length and format of submissions since banks' business and risk profiles differ. As such the ICAAP document should be proportional to the size, nature and complexity of a bank's business.

This format has been provided as a starting point. Banks are not required to adopt this format. However, adopting this format may be convenient for banks as it covers the minimum issues which typically would be the subject of review by the BSP and may therefore make the review process more efficient for both the bank and the BSP.

Equally, use of this template is not a substitute for being aware of the relevant rules.

What is an ICAAP document?

An ICAAP document is a bank's explanation to the BSP of its internal capital adequacy assessment process. While this may be based on existing internal documentation from numerous sources, the BSP will clearly find it helpful to have a summary prepared to communicate the key results and issues to it at a senior level. Since the BSP will be basing many of its views on the information contained in the ICAAP document, the bank's board of directors and senior management should have formally approved its contents. As such, the BSP would expect the ICAAP document to be in a format that can be easily understood at a high level and to contain all the relevant information that is necessary for the bank and BSP to make an informed judgment and decision as to the appropriate capital level and risk management approach.

Where appropriate, technical information on risk measurement and capital methodologies, and all other works carried out to validate the approach (e.g. board papers and minutes, internal or external reviews) could be contained in appendices.

1. EXECUTIVE SUMMARY

The purpose of the Executive Summary is to present an overview of the ICAAP methodology and results. This overview would typically include:

i. The purpose of the report and which group entities are covered by the ICAAP;

ii. The main findings of the ICAAP analysis:

- How much and what composition of internal capital the bank considers it should hold as compared with the capital adequacy requirement under the existing BSP Risk-Based Capital Adequacy Framework (the Framework), and
- The adequacy of the bank's risk management processes given the risks assumed;

iii. A summary of the financial position of the business, including the strategic position of the bank, its balance sheet strength, and future profitability;

iv. Brief descriptions of the capital and dividend plan; how the bank intends to manage capital going forward and for what purposes;

v. Commentary on the most material risks, why the level of risk is acceptable or, if it is not, what mitigating actions are planned;

vi. Commentary on major issues where further analysis and decisions are required; and

vii. Who has carried out the assessment, how it has been challenged, and who has approved it.

2. BACKGROUND

This section would cover the relevant organizational structure and business lines, and historical financial data for the bank (e.g., group structure (legal and operational), operating profit, profit before tax, profit after tax, dividends, equity, capital resources held and as compared with regulatory requirements, total loans, total deposits, total assets, etc., and any conclusions that can be drawn from trends in the data which may have implications for the bank's future).

3. CAPITAL ADEQUACY

This section could start with a description of the risk appetite used in the ICAAP. It is vital for the BSP to understand whether the bank is presenting its view regarding: (1) the amount of capital required to meet minimum regulatory needs, or (2) the amount of capital that a bank believes it needs to meet its business objectives (e.g., whether the capital required is based on a particular desired credit rating, or includes buffers for strategic purposes, or minimizes the chances of breaching regulatory requirements). A description of the methodology used to assess the bank's capital adequacy should also be included.

The section would then include a detailed review of the capital adequacy of the bank.

The information provided would include:

Timing

i. The effective date of the ICAAP calculations together with consideration of any events between this date and the date of submission which would materially impact the ICAAP calculation together with their effects; and

ii. Details of, and rationale for, the time period over which capital has been assessed.

Risks analyzed

i. An identification of the major risks faced in each of the following categories:

- credit risk;
- market risk;
- interest rate risk in the banking book;
- liquidity risk;
- operational risk;
- compliance risk;
- strategic/business risk; and
- reputation risk;

ii. And for each, an explanation of how the risk has been assessed and, where appropriate, the quantitative results of that assessment;

iii. Where relevant, a comparison of that assessment with the results of the assessment under the Framework (specifically for credit risk, market risk, and operational risk);

iv. A clear articulation of the bank's risk appetite by risk category if this varies from the assessment; and

v. Where relevant, an explanation of any other methods apart from capital used to mitigate the risks.

The discussion here would make clear which additional risks the bank considers material to its operation and, thus, would warrant additional capital on top of that required for credit risk, market risk, and operational risk under the Framework.

Methodology and assumptions

A description of how assessments for each of the major risks have been approached and the main assumptions made.

At a minimum, the BSP expects banks to base their ICAAP on the results of the capital adequacy requirement under the

Framework and additional risks, where applicable, should be assessed separately.

Capital transferability

Details of any restrictions that may curtail the management's ability to transfer capital into or out of the business(es) covered, for example, contractual, commercial, regulatory or statutory restrictions that apply.

4. CURRENT AND PROJECTED FINANCIAL AND CAPITAL POSITIONS

This section would explain the current and expected changes to the business profile of the bank, the environment in which it expects to operate, its projected business plans (by appropriate lines of business), and projected financial position for, say three to five years.

The starting balance sheet and date as of which the assessment is carried out would be set out.

The projected financial position might consider both the projected capital available and projected capital resource requirements to support strategic/business initiatives. These might then provide a baseline against which adverse scenarios (please see Capital Planning below) might be compared.

Given these business plans, this section would also discuss the bank's assessment on whether additional capital is necessary on top of that assessed to cover their existing risk exposures, as well as future planned sources of capital.

5. CAPITAL PLANNING

This section would explain how a bank would be affected by an economic recession or downswings in the business or market relevant to its activities. The BSP is interested in how a bank would manage its business and capital so as to survive a recession/ market disruption while meeting minimum regulatory standards. The analysis would include financial projections forward for, say, three to five years based on business plans and solvency calculations. Likewise, a bank should disclose here the key assumptions and other factors that would have significant impact on its financial condition, in conducting scenario analyses/ stress testing.

Typical scenarios would include how an economic downturn/market disruption would affect:

i. the bank's capital resources and future earnings; and

ii. the bank's capital adequacy requirement under the Framework taking into account future changes in its projected balance sheet.

It would also be helpful if these projections showed separately the effects of management potential actions to change the bank's business strategy and the implementation of contingency plans.

In addition, banks are encouraged to include an assessment of any other capital planning actions that would be necessary to enable it to continue to meet its regulatory capital requirements throughout a recession/market disruption such as new capital injections from related companies or new share issues.

Given the projected capital needs arising from an economic recession or business/market downswings, this section would also discuss the bank's assessment on whether additional capital is necessary on top of that assessed to cover their existing risk exposures and business plans.

6. CHALLENGE AND ADOPTION OF THE ICAAP

This section would describe the extent of challenge and testing of the ICAAP. Banks should describe the review and sign-off procedures used by senior management and the board. It might also be helpful if a copy of any relevant report to senior management or the board and their response were attached.

Details of the reliance placed on any external suppliers would also be detailed here, e.g. for generating economic scenarios.

In addition, a copy of any report obtained from an external reviewer or internal audit would also be included.

7. USE OF THE ICAAP WITHIN THE BANK

This section would describe the extent to which capital management is embedded within the bank including the extent and use of scenario analysis and/or stress testing within the bank's capital management policy, e.g. in business decisions (e.g. expansion plans) and budgets, or in allocating capital to business units, or in individual credit decision process.

Banks should include a statement of the actual operating philosophy on capital management and how this links to the ICAAP. For instance differences in risk appetite used in the ICAAP as compared to that used for business decisions might be discussed.

Lastly, it would be helpful if details on any anticipated future refinements within the bank's ICAAP (highlighting those aspects which are work-in-progress), as well as any other information that would help the BSP review the bank's ICAAP could be provided.

(Circular No. 639 dated 15 January 2009)

Annex B

ALTERNATIVE INTERNAL CAPITAL ADEQUACY ASSESSMENT PROCESS METHODOLOGIES

This appendix outlines ICAAP methodologies which banks may adopt in lieu of that based on the minimum regulatory capital requirement under the BSP Risk-Based Capital Adequacy Framework (the Framework). However, the choice of methodology should clearly be commensurate with banks' ability to collect the necessary information and to calculate the necessary inputs in a reliable manner.

Structured approach - In this case, banks will need to set the internal capital requirement at a starting point of zero capital and then build on capital due to all risks (both those captured under the Framework and those that are not) and external factors. This methodology could be seen as a simple model for calculating economic capital and is not based on the minimum regulatory capital requirement. A sensitivity analysis could form the starting point. The sensitivity analysis should be based on an exceptional but plausible scenario. Risks which are not included in the sensitivity analysis should also be considered in terms of the structured approach.

Allocation-of-risk-taking approach – In this approach, banks might start with its actual capital and break it down to all its material risks. This step in the process requires quantification or at least an estimation method for various risks. The amount of capital provided for each risk category is determined by the current and envisaged amount of risk in each category, a risk buffer and their risk appetite. Banks will decide which type of risk quantification/ estimation method is suitable and sufficient for its particular use. If the allocated capital seems insufficient, either the risk has to be reduced or capital has to be raised. The allocated amounts of the capital will therefore work as a limit system, which assists and facilitates banks in balancing their risk-taking capacity and their risks.

Formal economic capital models – These are expected to be used eventually by banks that use advanced approaches in determining the minimum regulatory capital requirement, or those that have substantial derivatives and structured products transactions (i.e., those that have expanded dealer and/or user capabilities).

(Circular No. 639 dated 15 January 2009)

GUIDELINES ON THE BANGKO SENTRAL'S SUPERVISORY REVIEW PROCESS

(Appendix to Sec. 4119Q)

A. Introduction

1. The BSP's supervisory review process (SRP) in the context of this document involves (1) an evaluation of banks' internal capital adequacy assessment processes (ICAAP) and their output, (2) a dialogue with banks with regard to their ICAAP, and (3) the prudential measures that may be taken to address issues identified. These guidelines should be observed mainly by the appropriate Central Point of Contact Department (CPCD) within the BSP and, where appropriate for on-site validation during regulation examination, by the examination personnel. This therefore supplements the existing guidelines set out in the Manual of Examinations, the CAMELS Rating, and the Risk Assessment System (RAS). The CPCD may draft, for its own use, detailed guidelines on the conduct of the assessment of banks' ICAAP and of the BSP-bank dialogue.

2. Although these guidelines are directed mainly at BSP supervision and examination personnel, banks will have a clear interest in knowing the approach the BSP intends to take in assessing their capital adequacy.

B. Guiding principles in assessing banks' ICAAP

1. As a first step, the BSP should evaluate banks' compliance with the minimum regulatory capital requirements as prescribed under the Framework. This would involve the verification of banks' calculation of their risk weighted assets (RWA) and capital adequacy ratio (CAR). The minimum regulatory capital requirements should always be the starting point in the assessment of banks' capital adequacy. The validated CAR should then be compared with the required capital resulting from the ICAAP.

2. Next, the assessment of banks' ICAAP should include an evaluation of their assumptions, components, methodologies, coverage and outcome. This review should cover both banks' risk management processes and their assessment of adequate capital. The BSP should review how banks assess the other risks they are exposed to, especially Elements 2 to 4 listed in Item "*C.4*" hereof, the controls they have in place to mitigate these risks, as well as the adequacy and composition of capital held against those risks.

3. The BSP should then identify existing or potential problems and key risks faced by banks, the deficiencies in their control and risk management frameworks, and the degree of reliance that can be placed on the outputs of their ICAAP. This process will enable the BSP to tailor its approach for each individual bank and will provide the foundation for the BSP's general approach for each bank and its actions.

4. The BSP's evaluation of the adequacy of banks' capital in relation to their risk profile would serve as the basis for assigning a rating for the Capital component of the bank's CAMELS rating. It would also serve as the basis for identifying any prudential measures or other supervisory actions required. For example, where there is an imbalance between business and risk controls, the BSP should consider the range of remedial supervisory actions that may be needed to rectify a deficiency in controls and/or perceived shortfalls in capital, either as a long-term requirement(s) or as a short-term action(s).

5. The results of the SRP will be communicated to the board and senior

management of banks together with any action that is required of them and any significant action planned by the BSP. This may be done as part of the dialogue between the BSP and each bank on the ICAAP.

6. In evaluating the ICAAP of branches of foreign banks in the Philippines, the BSP will refer to the home supervisor's consolidated assessment of the ICAAP of the head office/parent bank. The BSP will also take into account the strength and availability of parental support.

C. Guiding principles on BSP-bank dialogue

1. A key element of the SRP is the dialogue between the BSP and each bank. The dialogue will inform the BSP about the way each bank's ICAAP is structured, and the assumptions and methodologies which are used to assess its risk exposures.

2. The ICAAP document, which banks are required to submit to the BSP every January of each year (suggested format is in *Annex A* of *Appendix 91*), will be the basis for the BSP-bank (specifically, BSP-CPCD) dialogue. This dialogue may feed into the regular examination, and the findings of the regular examination may in turn feed into the dialogue. The BSP will determine the nature and depth of the dialogue, based on the type and complexity of the bank.

3. Banks should be able to justify their processes for identifying and measuring their risks as well as how much capital, if any, they allocate against them, taking into account other qualitative mitigants of risk. Banks should be able to explain any differences between their own assessment of capital needs and targets under the ICAAP and the minimum regulatory capital requirements prescribed under the Framework.

4. The dialogue should embrace the following four main elements:

a. Element 1: Risks covered under the Framework (i.e., credit risk, market risk, and operational risk);

b. Element 2: Risks *not fully* covered under the Framework (for example, credit concentration risk, risk posed by non-performing assets, risk posed by contingent exposures, etc.);

c. Element 3: Risks *not* covered under the Framework (other risks identified under Circular No. 510 dated 3 February 2006); and

d. Element 4: External factors, which include risks which may arise from the regulatory, economic or business environment.

5. Aside from these four main elements, the dialogue should also cover the quality of internal governance of banks, including risk controls, compliance and internal audit, as well as operational and organizational structure.

6. For the SRP to be effective, the BSP will need to develop a sufficiently thorough understanding of how the ICAAP is determined and the differences between it and the minimum regulatory capital requirement under the Framework. This would help in evaluating the ICAAP outcome. The SRP emphasizes the importance of analyzing the main elements, and understanding the differences between ICAAP assumptions and minimum regulatory capital requirement assumptions.

7. Once the process has begun, the dialogue will provide the opportunity for iteration between the ICAAP and SRP, with each informing the other, i.e., banks may make changes to the ICAAP in the course of the dialogue, in response to challenge and feedback from the BSP, and vice versa. Following the dialogue, the BSP will reach an assessment.

D. Guidelines on prudential measures

1. If the BSP considers that a bank's ICAAP does not adequately reflect its overall

risk profile, or does not result in the bank having adequate capital, then consideration should be given to applying prudential measures.

2. The measures available to the BSP include:

a. Requiring the bank to improve its internal control and risk management frameworks;

b. Requiring the bank to reduce the risk inherent in its activities, products and systems;

c. Restricting or limiting the business, operations or network of the bank;

d. Limiting or prohibiting the distribution of net profits and requiring that part or all of the net profits be used to increase the capital accounts of the bank; and

e. Requiring the bank to increase its capital.

3. The choice of prudential measures should be determined according to the severity and underlying causes of the situation and the range of measures and sanctions available to the BSP. Measures can be used individually or in combination. The requirement to increase capital should, however, be imposed on any bank which exhibits an imbalance between its business risks and its internal control and risk frameworks, if that imbalance cannot be remedied by other prudential measures or supervisory actions within an appropriate timeframe.

4. The requirement to increase capital may also be set where the BSP judges the existing capital held by a bank to be inherently inadequate for its overall risk profile. It must be acknowledged that there is no 'scientific' method for determining the amount, and that capital is not a long-run substitute for remedying deficiencies in systems and controls. In practice, the process relies heavily on subjective judgment and peer-group consistency to ensure a level playing field and a defense to possible challenge that may be posed by banks.

5. Prudential measures should be communicated promptly and in sufficient detail. In communicating its decision on prudential measures, the BSP should:

a. Explain in sufficient detail the factors which have led to the risk assessment conclusions;

b. Indicate areas of weakness and the timeframe for remedial action;

c. Explain the reasons for any additional capital requirement; and

d. Indicate what improvements could be made to systems and controls to make them adequate for the risks and activities of the bank, and for this improvement to be reflected in the bank's capital requirements.

(Circular No. 639 dated 15 January 2009)

App. Q-54
10.12.31

PROCESSING GUIDELINES FOR MICROFINANCE OTHER BANKING OFFICES OR MICROBANKING OFFICES

(Appendix to Subsection 4160Q.3)

The establishment of other banking offices and the notes on microfinance shall be guided by the following processing guidelines:

The processing of applications will be undertaken in a two-stage process.

Stage 1: Letter of Intent and Pre-qualification

Stage 2: Business Plan (Strategic and Operational Plan Assessment)

Stage 1: The applicant QB shall submit a letter of intent duly authorized by the Board of Directors, signed by the President or equivalent rank. The letter will be evaluated by the appropriate Supervision and Examination Sector (SES) Department based on safety and soundness considerations.

Stage 2: The applicant QB will be required to submit a business plan containing the strategic and operational details. Among others, such plan shall address the following questions:

1.Why is the QB establishing micro-banking offices and how does it relate to the overall corporate strategy?

2. How many are to be established in the next 1 (one) year, 3 (three) years, 5 (five) years? Where are these to be established? Why have these areas been identified?

3. What are the products and services to be offered?

4. How is the expansion to be funded?

5. How does the QB plan to maintain adequate command and control over the expanded network?

6. The proposed MBOs are to be linked operationally to which branches?

7. How does the QB propose to comply with the minimum fifty percent (50%) microfinance transaction requirement per MBO? (Microfinance transactions comprise of micro-loans and micro-deposits)

8. What is the policy on the minimum cash position of the MBO? This shall include arrangement for replenishment.

9. What are the management and organizational arrangements for the MBO? This shall include proposed staffing pattern and functions and qualification of the personnel in accordance with the requirements in 4160Q.3.

10. What are the Management Information Systems (MIS) and financial accounting arrangements to support customer handling and proper recording and reporting of transactions?

11. What are the physical security arrangements? These arrangements shall be included in the overall security program of the bank.

A final decision will be made based on the quality of Stage 2 submissions. Stage 2 submissions will be evaluated whether the proposed operational plan is commensurate and proportionate to the strategy to ascertain safe and sound MBO operations. A QB may apply for additional MBOs, after six (6) months from approval of the initial set/batch. All MBOs must be opened within one (1) year from their approval. If not deemed satisfactory, the application may be denied. Re-application shall only be allowed after six (6) months from the date of receipt of denial.

All applications are to be submitted through the Central Application and Licensing Group (CALG) of the SES.

(M-2010-040 dated 04 November 2010)

GUIDELINES ON OUTSOURCING OF SERVICES BY ELECTRONIC MONEY ISSUERS (EMIs) TO ELECTRONIC MONEY NETWORK SERVICE PROVIDERS (EMNSP)

(Appendix to Subsec. 4780Q.11)

I. *Statement of policy*. It is the goal of the BSP to achieve a truly inclusive financial system. In line with achieving this goal, the BSP recognizes the potential of electronic money (e-money) as an instrument to facilitate delivery of financial services affordably to the low-income, unbanked or undeserved segments of the population, particularly in non-urbanized areas. The BSP likewise recognizes that efficient and effective delivery of financial services may necessitate Electronic Money Issuers (EMI) to develop business models that utilize outsourcing arrangements, considering the specialized operational and technological requirements in an e-money business. Outsourcing, however may introduce an EMI to certain operational and reputational risks that need to be properly managed. The BSP hereby issues the following guidelines to govern the outsourcing of E-Money related services.

II. *Definition*. An Electronic Money Network Service Provider (EMNSP) shall refer to a non-financial institution that provides automated systems, network infrastructure, including a network of accredited agents utilizing the systems, to enable clients of an EMI to perform any or all of the following:

a. Convert cash to e-money and monetize e-money;

b. Transfer funds from one electronic wallet to another;

c. Use e-money as a means of payment for goods and services; and

d. Conduct other similar and/or related e-money activities/transactions.

III. *Application to outsource*. An EMI intending to outsource the services contemplated under Item *"2"* shall limit itself to an EMNSP as an outsource entity, and shall follow the procedures for outsourcing information technology systems/processes as provided under *Appendix Q-37*. In addition to the documentary requirements under said Subsec., an EMI should also submit a certification signed by its President or any officer of equivalent rank and function certifying that a due diligence review had been conducted and that the selected EMNSP has met the minimum requirements provided under Item *"V"*.

IV. *Responsibilities of an EMI*. Relative to the outsourcing of services to an EMNSP, it shall be the responsibility of an EMI to:

a. Conduct due diligence review on an EMNSP in accordance with Item *"V"*;

b. Ensure that the relationship/ arrangement with an EMNSP is supported by a written contract that should contain, at a minimum, the requirements prescribed under *Appendix Q-37*. The contract should also stipulate that:

(1) the EMNSP shall allow the BSP to have access and to examine the e-money system, network infrastructure, operation of the network of accredited agents and all operations related to e-money services being outsourced by the EMI for the purpose of assessing the confidentiality, integrity, and reliability of the e-money system and determining compliance with BSP rules and regulations;

(2) that the EMNSP shall not further outsource or subcontract the activity being outsourced to the EMNSP; and

(3) that interconnection by the EMNSP with other networks shall be limited to networks of other EMNSPs and the BSP-recognized ATM consortia.

c. Ensure that the EMNSP employs a high degree of professional care in performing the outsourced activities as if these were conducted by the EMI itself. This would include, among others, making use of monitoring and control procedures to ensure compliance at all times with applicable BSP rules and regulations;

d. Ensure that the EMNSP has an accreditation process in the selection of agents participating in the retail network for the conversion of cash to e-money and its monetization and that the EMNSP has instituted mechanism to manage sufficient liquidity in the system/network.

e. Ensure that the EMNSP enforces a program that requires all cash-in and cash out agents under its network to undergo AML trainings and re-trainings every two (2) years; and

f. Comply with all laws and BSP rules and regulations covering the activities outsourced to the EMNSP, especially on compliance with anti-money laundering (AML) requirements.

V. *Due diligence and continuing operational review*. Prior to entering into an outsourcing arrangement with an EMNSP, an EMI should conduct appropriate due diligence review to assess the capability of an EMNSP in performing the service to be outsourced. The due diligence should take into consideration both qualitative and quantitative factors affecting the performance of the outsourced service, such as the financial condition and results of operation for the previous year/s, risk management practices, technical expertise which involve monitoring the velocity of e-money transactions and aggregation of monthly limits, among others, market share, reputation (both the company and its stockholders) and compliance with anti-money laundering requirements and BSP rules and regulations.

An EMI should make sure that the EMNSP adheres to international standards on IT governance, information security, and business continuity in the performance of its outsourced activities. An EMI should endeavor to obtain independent reviews and market feedback on the EMNSP to supplement its own findings.

Operational review by an EMI of the EMNSP should be undertaken at least on an annual basis as part of risk management. This review should be documented as part of an EMI's monitoring and control process.

VI. *Delineation of responsibilities*. The EMI and EMNSP shall identify, delineate and document the responsibilities and accountabilities of each party as regards the outsourcing arrangement, including planning for contingencies. Notwithstanding any contractual agreement between an EMI and an EMNSP on the sharing of responsibility, the EMI shall be responsible to its customers, without prejudice to further recourse, if any, by the EMI to the EMNSP.

VII. *Confidentiality and security*. An EMI should review and monitor the security practices and control processes of the EMNSP on a regular basis, including commissioning or obtaining periodic expert reports on adequacy of security to maintain the confidentiality and integrity of data, and compliance with internationally-recognized standards in respect to the operations of the EMNSP. Considering that the EMNSP may service more than one EMI, the EMI should ensure that records pertaining to its transactions are segregated from those of other EMIs.

The EMI and EMNSP shall identify circumstances under which each party has the right to change security requirements. An EMNSP should be required to report immediately any security breaches to the EMI.

In addition, the EMI should make sure the EMNSP have documented business continuity plans in place and that said plan is periodically reviewed and tested with no significant test findings. An EMNSP shall provide the EMI with timely and adequate notification on any adverse development that may impact the former's performance and delivery of service to the EMI.

VIII. *EMI-Others intending to be an EMNSP*. An EMI-Others that intend to be an EMNSP because of its specialized technical expertise shall comply with the requirements for an EMNSP. In addition, an EMI-Others shall undertake risk-mitigating measures to ensure that liquid assets, corresponding to the outstanding balance of e-money issued by the EMI-Others and maintained pursuant to Sec. 4780Q and Subsecs. 4780Q.1 to 4780Q.7, be insulated from risks arising from its liabilities as EMNSP. These measures may include ring fencing the liquid assets through an escrow or trust account in a financial institution acceptable to BSP.

IX. *Sanctions*. Violations committed by EMIs pertaining to outsourcing of activities to EMNSP shall be subject to monetary penalties as graduated under *Appendix Q-39* and/or other non-monetary sanctions under Section 37 of RA No. 7653.

X. *Transitory provisions*. EMIs that were granted an authority to outsource their e-money activities to an EMNSP may continue to exercise such authority provided that they have to conform to this guidelines within a six (6)-month period from 04 Novemeber 2010.

(Circular No. 704 dated 22 December 2010)