



MEMORANDUM – 2013-012

To : All Market Participants and the Investing Public

Subject : Proposed Amendment to the Rules of the Capital Markets Integrity Corporation

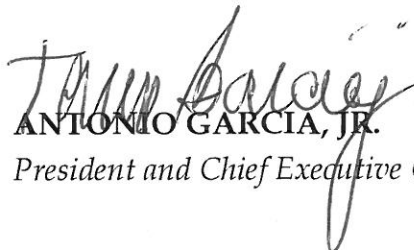
Date : 14 May 2013

Please be advised that in a letter dated 8 April 2013, the Securities and Exchange Commission ("SEC") directed the Capital Markets Integrity Corporation ("CMIC") to post and disseminate, through the PSE website, the proposed amendments to the CMIC Rules.

The proposed amendments were approved by the Board of Directors of CMIC last 28 November 2012 to strengthen the implementation, as well as enhance the effectiveness, of the current CMIC Rules. The proposed amendments are also intended to clarify some provisions of the CMIC Rules and harmonize them with the provisions of the Securities Regulation Code, its Implementing Rules and Regulations, the rules of the Philippine Stock Exchange, and other relevant securities laws, rules and issuances of the SEC.

In compliance with the said directive, we are posting herewith, for public comments, the draft of the proposed Amended CMIC Rules, with the proposed amendments underscored for easy reference. Kindly put your comments in writing and send to CMIC at Unit 27-E1, 27th Floor, Tower One & Exchange Plaza, Ayala Avenue, Makati City, or through email at info@cmic.com.ph. CMIC will receive comments on the draft proposed amendments until **31 May 2013**.

For information.


ANTONIO GARCIA, JR.
President and Chief Executive Officer



CAPITAL MARKETS INTEGRITY CORPORATION RULES

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ARTICLE I. GENERAL PROVISIONS

Section 1. *Statement of Objectives.* **CMIC** shall maintain the highest code of ethics, honor and integrity among its Trading Participants, establish, promote and indicate just and equitable principles of trade and business, and maintain the highest standards in the commercial and financial transactions of its Trading Participants among themselves and with the government and the public.

CMIC shall maintain the integrity of the market and minimize the risk of the investing public by ensuring that Trading Participants adhere to all rules and code of conduct of **CMIC** and all related legislative and regulatory requirements.

Section 2. *Definitions.* (a) In these Rules, the following capitalized words and expressions shall, unless the context requires otherwise, have the meanings ascribed to them hereunder:

“Associated Person” shall refer to a person who directly exercises control of supervisory authority, but does not include a salesman, or an agent or a person whose functions are solely clerical or ministerial.

“Clearing Agency” shall mean a clearing agency duly registered in accordance with the SRC and SRC Rules and designated by the Exchange as its clearing agency.

“CMIC” shall mean the Capital Markets Integrity Corporation.

“Code” shall mean the Securities Regulation Code.

“Commission” shall mean the Securities and Exchange Commission of the Philippines.

“Complaint” shall mean any written statement of a customer or any other interested party alleging a grievance involving the business of a Trading Participant or Issuer or a violation of the Securities Laws by a Trading Participant or Issuer.

“Days” shall mean trading days in the Exchange.

“DD” shall mean the Disclosure Department of the Exchange.

“Done Through Account” shall mean an account which a Trading Participant maintains with another Trading Participant and uses to effect transactions for its customers.

“Examination Findings” shall mean any violation of the Securities Laws and these Rules as determined during an examination conducted by CMIC.

“Examinee” shall mean a Trading Participant under examination or investigation by CMIC.

“Exchange” or “PSE” shall mean the Philippine Stock Exchange, Inc.

“Issuers” shall mean the companies whose securities are listed in the Exchange.

“ITD” shall mean the Information Technology Division of the Exchange.

“LD” shall mean the Listing Department of the Exchange.

“Risk Based Capital Adequacy Ratio” or “RBCA Ratio” shall refer to the minimum level of capital that has to be maintained by firms which are licensed, or securing a Broker Dealer license, taking into consideration the firm size, complexity and business risk. Such risks that are considered in determining the capital requirement include, among others, operational, position, counter-party, large exposure, underwriting, and margin financing risks.

“Rules” shall mean the CMIC Rules for PSE Trading Participants.

“Securities Laws” shall mean the Securities Regulation Code (“SRC”), its implementing rules and regulations (the “SRC Rules”), and the rules (including these Rules), circulars, directives and/or other issuances of the Commission or CMIC to govern Trading Participants, Issuers and other market participants.

“Secured Demand Note Agreement” shall mean a notarized agreement (including the related secured demand note) entered into by a Broker Dealer as borrower and a lender, evidencing or governing the contribution of a secured demand note to a Broker Dealer and the pledge of securities and/or cash with the Broker Dealer as collateral to secure payment of such secured demand note.

“SIPF” shall mean the fund under the Securities Investors Protection Fund, Inc.

“Subordination Agreement” shall mean either a subordinated loan agreement or a secured demand note agreement.

“Subordinated Loan Agreement” shall mean a notarized agreement evidencing or governing a subordinated borrowing of cash.

“Trading Halt” shall mean the temporary stoppage of the trading of a listed security in the Exchange.

“Trading Participants” shall mean brokers and/or dealers duly licensed by the Commission and authorized to exercise a Trading Right pursuant to the rules of the Exchange. Unless the context requires otherwise, the term shall include directors, officers, Associated Persons, Salesmen and other agents of Trading Participants.

“Trading-related Irregularities” shall mean any violation of Sections 24, 25, 26 and 27 of the Securities Regulation Code and their implementing rules and regulations (including SRC Rules 24.1(b)-1, 24.1(d), 24.2.2, 24.2-3, and 26.3), and Article XI-B of these Rules, including, but not limited to, manipulative and fraudulent practices and insider trading.

“Unusual Trading Activities” shall mean any abnormal movement in the price and/or trading volume in the market of a listed security as may reasonably give rise to suspicion of a Trading-related Irregularity.

(b) Unless the context requires otherwise or unless otherwise defined herein, the terms used in these rules shall have the same meanings under the Securities Regulation Code and its implementing rules and regulations or other relevant rules of **CMIC** and the Exchange.

Section 3. *Enforcement and Observance of the Securities Laws.* CMIC shall enforce compliance by Trading Participants and, in the proper case, by Issuers with the Securities Laws. Trading Participants shall be bound by and observe the following laws, rules and regulations which, except for these Rules, are incorporated as integral parts hereof by reference:

- (a) The Securities Regulation Code and its implementing rules and regulations;
- (b) The Anti-Money Laundering Law and its implementing rules and regulations;
- (c) The Code of Conduct and Professional Ethics for Traders and Salesmen;
- (d) These Rules; and
- (e) Such other relevant laws and regulations.

Section 4. *Official Publications.* A Trading Participant shall state in its business letters, notices and other official publications or documents that it is a trading participant of The Philippine Stock Exchange, Inc., a member of SCCP and of the SIPF.

Section 5. *Reporting Obligation of Trading Participants.* Every Trading Participant shall prepare and file with **CMIC** such periodic, special or other reports, which the Securities Laws, the Commission, the Exchange or **CMIC** requires.

Every Trading Participant shall also prepare and file with CMIC, in such form and substance and within the period mandated by CMIC, such reports and other documents, which CMIC may order a Trading Participant to prepare and file to enforce compliance with the Securities Laws.

Section 6. *Reports to be Verified Under Oath.* Risk Based Capital Adequacy (RBCA) reports which a Trading Participant should prepare and file with CMIC under these Rules or the Securities Laws shall be verified under oath and signed by the President or the equivalent officer and the Associated Person; in case of financial reports and documents, the Chief Financial Officer or the equivalent officer (the "Executing Officers") of the Trading Participant. The verification shall state that:

- (a) The Executing Officers have read the relevant report or document;
- (b) Based on the Executing Officers' personal knowledge or based on authentic records, the statements in the report or document are true and correct;
- (c) The report or document does not contain any untrue statement of a material fact or omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which such statements were made, not misleading; and
- (d) Based on the Executing Officers' personal knowledge or based on authentic records, the financial statements, and other financial information included in the report or document, fairly present in all material respects the financial condition and results of operations of the Trading Participant.

Section 10. *Continuing Liability.* Subject to the relevant prescriptive period under the Code and other applicable laws, a Trading Participant shall not be relieved from any liability incurred while still in operation or be excused from the obligations to cooperate in an investigation even if it may cease to be registered or be stricken off the register by the Exchange for any reason whatsoever. The Trading Participant shall continue to be bound by these Rules and the Securities Laws with respect to any antecedent violation thereof by the Trading Participant.

ARTICLE II. INVESTIGATION AND RESOLUTION OF CASES BY CMIC

Section 1. *Jurisdiction of CMIC.* CMIC shall have the jurisdiction to investigate and resolve: (1) All violations of the Securities Laws or these Rules by Trading Participants, and; (2) Trading-Related Irregularities and Unusual Trading Activities involving Issuers, based on any of the following complaints, findings, reports or determinations:

(a) Written complaints filed directly with CMIC by customers, Trading Participants, or any aggrieved party for alleged violation of the Securities Laws or these Rules;

(b) Examination Findings of CMIC based on regular annual examinations or for cause examinations of Trading Participants;

(c) Reports of Trading-related Irregularities or Unusual Trading Activities; and

(d) Matters which CMIC has determined should be investigated and resolved to enforce the Securities Laws and these Rules, including matters referred to CMIC by the Commission, the Clearing Agency, and the DD.

Any Complaint or referral to CMIC for investigation and/or resolution should be sent in writing to CMIC President and should state the particulars of the Complaint or referral. CMIC may act on anonymous complaints or referrals provided these contain sufficient leads or particulars to enable the taking of further action.

Section 2. *Duty and Responsibility of Trading Participant &/or Issuer in Investigations.* A Trading Participant &/or an Issuer shall comply or cause compliance with any order of CMIC to (a) attend, (b) provide information, and/or (c) produce records and other documents under its control at any investigation or other proceedings of CMIC in connection with (a) any matter within CMIC's jurisdiction to investigate and resolve under these Rules or (b) CMIC's enforcement of the Securities Laws. These orders shall include, but shall not be limited to, CMIC orders for:

(a) Immediate production of accurate information on a Trading Participant's or Issuer's business and transactions in a format, electronic or otherwise, specified by the Exchange or CMIC;

(b) Immediate production of documents (which, for the purposes of these Rules, shall include anything in which information of any description is recorded) in the Trading Participant's or Issuer's possession, custody, power or control;

(c) Provision of answers and explanations to CMIC, and recording of such answers and explanations electronically or otherwise;

(d) Provision of information on any person who is to be, is or has been an employee, agent or engaged in **the business of the Trading Participant or Issuer**; and

(e) Maintenance of a sound financial position so as not to endanger the interest of the investing public.

A Trading Participant **or Issuer** shall be responsible to **CMIC** for the conduct of its agents. For purposes of these Rules, the acts and omissions of an agent of a Trading Participant **or Issuer** shall be deemed an act or omission of the Trading Participant **or Issuer**.

Section 3. *Delineation of Jurisdiction of the LD, the DD and CMIC over Issuers.* The LD or the DD shall have jurisdiction over violations by Issuers of the disclosure requirements under the Securities Laws and the continuing listing requirements of the Exchange. CMIC shall have jurisdiction over Trading-related Irregularities and Unusual Trading Activity involving Issuers. The CMIC and the LD or the DD shall have authority to jointly or separately investigate and resolve violations within their respective jurisdictions.

Section 4. *Procedure for the Investigation of Complaints Against Trading Participants.* An aggrieved or interested party (the "Complainant") may file a written Complaint with CMIC against any Trading Participant for Trading-related Irregularities or other violations of the Securities Laws within six (6) months from knowledge of its commission. The Complaint should conform to the Complaint form, which CMIC may prescribe from time to time. Failure to file a Complaint within the prescribed period shall bar the aggrieved or interested party from filing a Complaint with CMIC.

If CMIC determines the Complaint to be sufficient in form and substance to justify an investigation under these Rules, CMIC shall proceed with the investigation of the Complaint in accordance with the following procedure:

(a) Within two (2) days from CMIC's receipt of the Complaint, CMIC shall order the Respondent to submit to CMIC an answer to the Complaint within ten (10) days from receipt of a copy thereof.

(b) Complainant may file with CMIC a reply to Respondent's answer within five (5) days from receipt of a copy thereof.

(c) Respondent may file with CMIC a rejoinder to Complainant's reply within five (5) days from receipt of a copy thereof.

(d) The issues having been joined, CMIC shall then assess the merit of the Complaint based on the submissions of the parties. If the Complaint is without merit, CMIC shall immediately dismiss it. If the Complaint has merit,

CMIC shall meet the parties within five (5) days from the date of filing of the last pleading to discuss a possible amicable settlement, clarify matters raised in the Complaint, and allow the parties to introduce additional evidence on their behalf.

(e) The proceedings before CMIC shall be in the nature of informal administrative hearings and CMIC shall not be bound by technical rules.

(f) If the parties agree to amicably settle the Complaint, CMIC shall evaluate the amicable settlement to ensure compliance with the Securities Laws. **In case the parties cannot personally appear, their representative should come equipped with the proper special power of attorney or board resolution, as the case may be, with full power or authority to enter into a compromise agreement or settlement.** If the settlement is in order, CMIC shall dismiss the complaint, provided that the parties have complied with the terms of the settlement. If the parties do not agree to amicably settle the Complaint, CMIC shall consider the Complaint submitted for resolution with notice to the parties.

(g) At any stage of the proceeding and for the purpose of gathering additional evidence, CMIC may order a special examination of Respondent solely with respect to the subject matter of the Complaint. **CMIC may likewise require the parties to submit additional pleadings, documents and evidence, in addition to those provided in this section. CMIC may also call the parties for additional conferences whenever necessary in the discretion of CMIC.**

(h) As far as practicable, within ten (10) days from the conclusion of the meeting mentioned in Section 4 (e) above or the special examination of the Respondent under Section 4 (h) above, as the case may be, CMIC shall resolve the Complaint.

(i) At any stage in the proceeding, should the Complainant inform the CMIC in writing that he wishes to withdraw the Complaint, the CMIC shall dismiss the same, with notice to the Respondent.

(j) **Except for the Complaint, which CMIC will furnish the Respondent, copies of all pleadings filed by a party with CMIC shall be furnished by such party to the other party/ies in the case. CMIC will not accept any pleadings filed without proof of service of the same to the other parties to the case.**

CMIC shall complete the investigation and resolution of a Complaint within sixty (60) days from receipt thereof.

Section 5. *Procedure for Investigation and Resolution of Examination Findings.*

(a) Regular Audit. CMIC shall conduct a regular audit of all Trading Participants as follows:

(i) In the last quarter of each year, CMIC shall prepare and adopt a work program and schedule (the "Audit Program") for the regular audit (the "Audit") of all Trading Participants, **based on adopted Auditing Standard**, for the following year.

(ii) CMIC shall submit the Audit Program to the Commission on or before the 15th day of **March** of the relevant year for approval, **provided that any amendment to the calendar for audit shall be promptly provided to the Commission**.

(iii) Upon approval by the Commission of the Audit Program, CMIC shall issue a letter, which shall be addressed and presented to the Trading Participant at the start of the Audit, authorizing CMIC's Audit of the Trading Participant in accordance with the Audit Program.

(iv) CMIC shall conduct the Audit in accordance with the Audit Program to verify and ensure compliance by Trading Participant with the Securities Laws. CMIC shall emphasize, but shall not be limited to, the examination of the Trading Participant's compliance with the following rules:

- (1) Books and Records Rule;
- (2) Net Capital Rule/RBCA Ratio and other financial ratios necessary to determine adequate capital for operation;
- (3) Customer Protection Rule; and
- (4) Relevant provisions of the Securities Laws on the business conduct and sales practices of Trading Participants.

(v) The Trading Participant shall comply with the letter of authority issued by CMIC and shall make available to CMIC within the Trading Participant's principal office all relevant books, records and documents, which CMIC may deem necessary or appropriate for the prompt completion of the Audit in the shortest time possible. In the course of the Audit, the Trading Participant may provide CMIC copies of such books, records and documents. At the start of the Audit, CMIC shall inform the Trading Participant of the Audit Program. CMIC shall conduct the Audit in the most professional and expeditious manner so as not to unduly hamper the operations and activities of the Trading Participant.

(vi) CMIC shall prepare any initial Examination Findings on the Trading Participant before the conclusion of the Audit. CMIC shall then hold an exit conference with the President or the equivalent officer and Associated Person of the Trading Participant to discuss the initial Examination Findings and to give the Trading Participant the opportunity to comment thereon.

(vii) If the Trading Participant agrees with the Examination Findings, CMIC shall render a decision based thereon.

If the Trading Participant does not agree with the Examination Findings, CMIC shall decide whether it shall conduct a post examination to verify the comment or reply of the Trading Participant.

(viii) CMIC shall render a decision based on its Examination Findings or, in the proper case, the result of the post examination.

CMIC shall complete the Audit and any post examination, and shall render a decision based on the Examination Findings or result of the post examination within sixty (60) days from commencement of the Audit.

(b) Spot Audit and Submission of Client Information. (i) In addition to the Audit of the Trading Participants, CMIC may conduct a spot audit (the "Spot Audit") of a Trading Participant based on parameters, which CMIC may from time to time establish, including the Trading Participant's (1) net liquid capital level and variance, (2) RBCA Ratio and risk exposure, (3) reserve requirement deficiency, and (4) settlement failure. CMIC shall conduct the Spot Audit substantially in accordance with Section 5 (a) above, excluding items (i), (ii) and (iii) of Section 5 (a). The Spot Audit shall focus on the Trading Participant's RBCA Ratio and related financial matters, provided that CMIC may expand the scope of the Spot Audit as it may deem necessary.

(ii) Any Trading Participant subject of a Spot Audit shall submit to CMIC in electronic form the current list of its clients with their respective cash and securities position immediately upon receipt of CMIC's letter of authority for the Spot Audit and at the end of each month thereafter until CMIC directs otherwise upon the Trading Participant's rectification of the Examination Findings based on the Spot Audit.

Section 6. Procedure for the Investigation and Resolution of Incidence of Unusual Trading Activities or Trading-related Irregularities.

(a) As soon as CMIC shall have monitored that transactions (the "Subject Transactions") of a Trading Participant involving the listed securities of an Issuer constitute Unusual Trading Activities or possible Trading-related Irregularities, CMIC shall make a report thereon (the "Incident Report").

(b) Should CMIC find cause to further investigate the Subject Transactions based on the Incident Report, CMIC shall obtain additional information from the Trading Participant on the Subject Transactions necessary or appropriate to establish the commission of Trading-related Irregularities or other violations of the Securities Laws. CMIC may also issue a letter, which shall be addressed and presented to the concerned Trading Participant, (i) authorizing CMIC to examine the books and records of the Trading Participant and/or (ii) directing the Trading Participant to submit to CMIC, within five (5) days, the names of the beneficial owners of the listed securities involved in Subject Transactions and such other documents as may be deemed necessary.

(c) CMIC shall prepare a preliminary report (the "Preliminary Report") based on the further investigation of the Subject Transactions and the result of the examination of the books and records of the Trading Participant.

(d) Should CMIC determine based on the Preliminary Report the absence of Unusual Trading Activities and Trading-related Irregularities, CMIC shall forthwith terminate the investigation of the Subject Transactions and shall send written notice of such termination to the Trading Participant within ten (10) days.

(e) Should CMIC determine based on the Preliminary Report the existence of Unusual Trading Activities and the possible commission of Trading-related Irregularities, CMIC Head shall:

- (i) Notify in writing the relevant Trading Participant of said determination; and
- (ii) Order the Trading Participant to submit to CMIC, within five (5) days from receipt of the order, a written explanation of why said Trading Participant should not be held liable for Trading-related Irregularities or other violation of the Securities Laws based on Subject Transactions.

To facilitate the submission of the written explanation and other documents (the "Submissions") to CMIC, the relevant party may fax or e-mail the written explanation or other document to CMIC, provided that the party shall send the original thereof to CMIC within the prescribed filing period.

(f) CMIC shall evaluate the Submissions of the relevant parties. Should CMIC determine the absence of Unusual Trading Activities and Trading-related Irregularities, CMIC Head shall forthwith terminate the investigation of the Subject Transactions. Otherwise, CMIC shall conduct an informal hearing to allow the relevant parties to present additional evidence in support of the Submissions.

(g) As far as practicable, within ten (10) days from the termination of the informal hearing mentioned in Section 6 (f) above, CMIC shall render a decision on the liabilities of the parties for Trading-related Irregularities or other violations of the Securities Laws based on the Subject Transactions.

CMIC shall complete the investigation and resolution of any incidence of Unusual Trading Activities or Trading-related Irregularities within six (6) months from the start of the investigation.

Section 7. *Procedure for Investigation and Resolution of Matters under Section 1 (d), Article II.* CMIC shall substantially follow the applicable provisions of this Article II in the investigation and resolution of matters, which CMIC, pursuant to

Section 1, Article II, has determined should be investigated and resolved to enforce the Securities Laws and these Rules.

Section 8. *Effect of Failure to Decide within Given Period.* CMIC shall complete the investigation and resolution of all cases under its jurisdiction within the relevant periods set forth in these Rules. Failure of CMIC to do so shall be a ground for the dismissal of the case, unless (a) the CMIC Board, upon application by CMIC before the lapse of the relevant period, grants CMIC additional time to complete the investigation and resolution of the case or (b) such failure was not due to the fault of CMIC or, in the proper case, the Complainant.

Section 9. *Authentication of Proceedings and Identification of CMIC Officers and Agents.* Before the start of any investigation, examination, audit or other proceedings of CMIC, the relevant CMIC officers and agents shall present to the relevant party the written authorization by CMIC of the investigation, examination, audit or other proceedings. CMIC officers and agents shall also properly identify themselves through their Exchange Employee Identification Cards or, in the case of professionals deputized by CMIC, other appropriate identification cards.

ARTICLE III. DISPOSITION OF CASES

Section 1. *Coverage.* This article shall govern all disposition of cases which CMIC may examine, investigate and resolve under these Rules.

Section 2. *Authority to Decide Cases.* CMIC shall decide in the first instance all cases within CMIC's jurisdiction under Section 1, Article II following the procedures set forth in Article II.

Section 3. *Basis of CMIC Decisions.* CMIC shall decide all cases within its jurisdiction based solely on the evidence presented or gathered in the course of its investigation, examination, audit or other proceedings. CMIC shall weigh evidence for or against a party in accordance with the rule on substantial evidence in administrative investigations. Substantial evidence means such relevant evidence as a reasonable mind might accept as adequate to support a conclusion.

Section 4. *Confidentiality of Information.* CMIC shall not disclose any information that it receives, gathers or otherwise acquires in the course of its investigation, examination, audit or other proceedings except (a) to parties to the case (b) to members or representatives of the Commission (c) when required by law, **rule, regulation, subpoena or other similar legal processes,** (d) pursuant to a lawful court order, or **(e) or upon written request of any regulatory body having due jurisdiction over the parties.**

Section 5. *CMIC Decisions.* For minor violations, disciplinary sanctions imposed by CMIC shall be immediately executory. For major and grave violations CMIC shall impose the appropriate sanctions after due investigation.

Section 6. *Request for Reconsideration from CMIC Decisions.* An aggrieved party may seek reconsideration of a decision or action of CMIC within ten (10) business days from receipt of such decision or action, provided, however, that if the decision is a summary action under SRC Rule 39.E, the period of appeal shall be five (5) business days from receipt of the decision.

The request must be in writing, addressed to the CMIC Board, with proof of service to the adverse party, if any. No filing fee shall be required for the CMIC Board to consider the appeal.

The request shall be signed by the aggrieved party and shall set forth a concise statement of facts, the issues involved and the grounds relied upon. If necessary, the aggrieved party may attach thereto documents referred to in the written appeal.

Section 7. *Appeal of CMIC Decision to the Commission.* In cases involving grave and major violations, decisions of CMIC may be appealed to the Commission

within fifteen (15) calendar days from receipt of decision in accordance with SEC Memorandum Circular No. 10 (2010) entitled "Rules of Procedure on Appeals from Decisions from SROs."

Section 8. *Execution of CMIC Decisions.* The implementation of the decisions of CMIC shall be stayed pending resolution of the appeal to CMIC, except in cases involving minor violations, and in cases where the sanction imposed is suspension or expulsion. Should suspension or expulsion be the sanction imposed, the decision will immediately be executory even pending appeal to CMIC, unless the aggrieved party shall post a bond in such amount as may be fixed in the decision subject of the appeal. Any monetary penalty may be paid under protest.

The decision of CMIC shall be immediately executory upon its promulgation notwithstanding any appeal to the Commission, without prejudice to the right of the aggrieved party to secure an order from the Commission staying the execution of the appealed decision.

Section 9. *Submission of Decisions and Reports to the Commission.* On or before the 10th day following the end of the relevant month, CMIC shall submit to the Commission a monthly report on cases resolved and decided.

All decisions or actions of CMIC under these Rules shall be in writing, shall state the basis therefore and shall be furnished to CMIC Board for submission to the Commission in accordance with the immediately preceding paragraph.

The report to the Commission shall reflect the following information as applicable: (1) Names of the Trading Participant/s and the person/s allegedly responsible for the violations, with their designations; (2) Description of the nature of the violations with brief narration of the participation of the persons allegedly responsible of such violations; (3) Supporting documents.

Further, if the persons allegedly responsible for the violations have existing registration with the Commission (e.g. salesman), such fact shall be indicated in the report. In this case, the CMIC shall initiate proceedings to suspend or revoke such registration if warranted, without *prejudice* filing of criminal case.

If the persons allegedly responsible for the violations are not registered with the Commission, such fact shall be indicated in the report. In this case, the CMIC shall initiate a criminal case against such persons, if warranted.

Section 10. *Summary Actions under Section 5, Article I.* Notwithstanding Section 10 of this Article, actions taken by CMIC pursuant to Section 5, Article I shall be governed exclusively by Section 5, Article I. Appeals from summary actions shall be governed by Section 5 of Article III.

Section 11. *Endorsement of Investigation Report to Commission.* Whenever necessary or appropriate, especially in a case where CMIC does not have the jurisdiction to impose penalties on the party or parties to the case, CMIC shall

immediately endorse to the Commission the relevant findings and recommendations of CMIC for appropriate action by the Commission.

ARTICLE IV. EMPLOYEES OF TRADING PARTICIPANTS

Section 1. *Definition of Employee.* For purposes of this Article, “Employee” of a Trading Participant shall mean a natural person who is hired, directly or indirectly by the said Trading Participant, to perform activities related to its business in exchange for compensation. It shall include, but shall not be limited to salesmen, traders, dealers, Associated Persons, consultants and other officers, as well as apprentices and trainees, whether they are considered as regular, probationary, casual, or project-based by the Trading Participant.

Section 2. *Registration of Salesmen and Associated Persons of Trading Participants.* A person shall not be employed as a Salesman or Associated Person of a Trading Participant unless the required registration as such is secured from the Commission.

Every person registered as a Salesman or Associated Person shall file the appropriate registration renewal form with the Commission and renew his license on an annual basis. Nevertheless, a Salesman’s registration shall cease to be effective upon his resignation or termination of employment with the Trading Participant.

Section 3. *Signing of Pledge of Commitment.* All salesmen, traders, dealers, agents and Associated Persons are mandated to sign the CMIC’s Pledge of Commitment and abide by the Code of Ethics for Salesmen and Traders. **A copy of the Pledge of Commitment must be submitted to CMIC no later than the first Friday of January of each year.**

Section 4. *Submission of List of Directors, Officers, Agents and Employees.* Trading Participants shall submit to CMIC a complete list of all directors, agents and Employees, including their respective positions, addresses and contact numbers, not later than the first Friday of January and July of each year. For newly approved Trading Participants, the said list, together with the Personnel Information Sheet of each director, agent or Employee, shall be submitted to CMIC prior to commencement of their trading operations. The list may be in printed or electronic form, as may be required by CMIC.

Section 5. *Director, Officer, Agent or Employee Movement.* Trading Participants shall notify CMIC of any director, officer, agent or Employee movement, whether hiring, resignation, re-designation, or termination of employment, within 30 days from effectivity thereof.

Section 6. *Clearance of Resigned and Terminated Agents and Employees.* A resigned or terminated Agent or Employee of a Trading Participant shall be given written clearance to join another Trading Participant by its former employer prior to the effectivity of his new employment.

However, a Trading Participant may withhold clearance from a former agent or Employee who:

- (a) has pending liabilities and obligations with the Trading Participant,
- (b) is involved in a pending case for any violation of Securities Laws,
- (c) was terminated for having violated rules, regulations or policies of the Trading Participant, or
- (d) has violated any provision of his employment contract with the Trading Participant.

The Trading Participant shall notify in writing the agent or Employee whose clearance has been withheld within thirty (30) days from the date of his resignation or termination, and furnish the CMIC with a copy of the same. Otherwise, the resigned or terminated agent or Employee is deemed to have been cleared, and may join another Trading Participant. The written notice shall state the reason why the clearance has been withheld and if applicable, the pending liabilities and obligations that the agent or Employee must satisfy in order for the clearance to be issued.

An agent or Employee whose clearance has been validly withheld cannot be employed as an agent or Employee, whether directly or indirectly, by another Trading Participant until after the lapse of six (6) months from the effectivity of his resignation or termination.

Section 7. Director, Officer, Agent or Employee Restrictions. Notwithstanding the above provision, the CMIC shall consider as unfit to be a director, officer, agent or employee of a Trading Participant, a person who has been convicted by a competent judicial or administrative body of an offense involving moral turpitude, fraud, embezzlement, counterfeiting, theft, estafa, misappropriation, forgery, bribery, false oath, or perjury, or of a willful violation of securities, commodities, banking, real estate or insurance laws.

In determining whether an individual is fit to be a director, officer, agent or employee of a Trading Participant, his integrity, experience, education, training and competence shall be considered.

Section 8. Publication of List of Directors, Officers, Agents and Employee Movement. The list of newly hired, resigned, re-designated or terminated directors, officers, agents and Employees of Trading Participants shall be circularized by CMIC every first week of the month and shall be posted on the PSE and CMIC websites for seven (7) calendar days.

Section 9. Penalty for Violation of the Policy on Hiring and Termination of Employees. Trading Participants shall abide by the provisions of this Article at all times. Violation of any provision of this Article shall be considered as a minor violation under the Sanctions Guidelines Table in Article XII.

ARTICLE V. CODE OF CONDUCT AND PROFESSIONAL ETHICS FOR TRADERS AND SALESMEN

Section 1. *General Principles.* The following general principles shall guide traders and salesmen in their professional and business dealings in the Exchange:

(a) Traders and salesmen should adhere at all times to the principles of honesty, integrity, fairness and good business practice in the conduct of their business affairs.

(b) As professionals, traders and salesmen should always strive to gain more knowledge of the market and to improve their trade skills and know-how.

(c) As responsible persons, traders and salesmen should not buy and/or sell or cause any other person to buy and/or sell any security in relation to which they have acquired non-public material information that would give them undue advantage vis-à-vis the general investing public.

(d) While traders and salesmen are free to manage their own investments, subject to the approval of the Associated Person, they shall not hype or otherwise manipulate any security to the prejudice of the investing public, their companies, the Exchange and/or **CMIC**.

(e) A trader or salesman must not enter into any transaction or act in any manner under any circumstance which would otherwise adversely affect his duties to the investing public, his company, the Exchange, **CMIC** or the Commission.

(f) Traders and salesmen should ensure that the assets of their clients are properly accounted for and adequately safeguarded.

Section 2. *Relationship of Traders and Salesmen to their Clients.* The following principles shall govern the relationship of traders and salesmen, and their clients:

(a) Traders and salesmen should always bear in mind that their clients' interest is paramount at all times and under no circumstance, either by a trader's or salesman's act or omission, shall it be prejudiced.

(b) Transactions that may involve conflicts of interest should be avoided, but when they cannot possibly be avoided, a trader or salesman should ensure that the client's interest is not subordinated to his own and his client is treated fairly before the transaction is executed. Fair treatment includes, but is not limited to, full disclosure to the client of all material facts related to a transaction involving conflict of interest.

(c) Traders and salesmen should exercise due diligence in determining their clients' financial situation, investment objectives, experience and risk tolerance.

(d) Traders and salesmen should exert reasonable efforts to keep their clients well-informed of relevant market news, disclosures and other developments in a timely and accurate manner. Corollarily, they must never fabricate information or spread groundless or false information about a particular security or the market.

(e) When providing advice to a client or prospective clients, traders and salesmen must make full, fair and express disclosure of all matters that could reasonably be expected to impair their independence and objectivity or interfere with respective duties to their clients.

These include, but are not limited to, relationships between an issuer and the trader or salesman, such as directorship or consultancy, investment banking, underwriting or financial relationships, broker/dealer market-making activities, and material beneficial ownership of stock.

(f) Traders and salesmen must disclose to their clients or prospective clients any compensation, consideration, or benefit received from or paid to others for the recommendation of products or services.

Section 3. *Relationship of Traders and Salesmen to their Firm.* The following principles should govern the relationship of traders and salesmen, and their firm:

(a) Traders and salesmen should act and carry themselves in a manner that would promote and maintain the integrity of their firm, in particular, and the market, in general.

(b) Traders and salesmen should observe all applicable regulatory laws, rules and regulations, comply with all regulatory requirements and abide by the internal rules of their firm at all times.

(c) A trader or salesman should be employed by only one Trading Participant at any given time.

Section 4. *Rules on Trading for One's Personal Account.* The following rules shall govern a trader's or salesman's transactions for his own personal account:

(a) **CMIC** shall allow traders and salesmen to deal for their own personal account on condition that they shall not abuse this privilege and that they will not enter into any transactions that would put their clients at a disadvantage.

(b) To ensure effective monitoring and surveillance, all personal transactions of traders and salesmen shall be transacted only through their own firm.

(c) A trader or salesman should use and maintain only one (1) personal dealing account, and only with his firm, which should be registered under his real name. Additionally, he is prohibited from having, opening or using a solo or joint account with any person in any other Trading Participant for the purpose of transacting securities.

(d) Traders' and salesmen's personal transactions shall require the prior written approval of their firm's Associated Person.

(e) The Trading Participant shall trade for its account only under a "Customer First Policy," and ensure the protection of the public and its clients.

Section 5. *Trading Participant Discretion to Prohibit Trading for One's Personal Accounts.* Notwithstanding Section 4 (a) above, a Trading Participant may prohibit their traders or salesmen from dealing in securities for whatever reason they may see fit. The discretion reserved to Trading Participants is unqualified and may not be questioned by traders and salesmen.

Section 6. *Prohibited Acts.* Traders and salesmen are prohibited from:

(a) Combining an order for their own account with client orders for the same security and handling both proprietary and client accounts.

(b) Entering into any securities transactions in their personal capacity with any client of their company, unless authorized by the Associated Person.

(c) Commingling the securities of a client with their own securities or commingling their securities with those of their clients.

(d) Sharing, directly or indirectly, in the profits or losses from trading in an account, other than their own, carried by the Trading Participant whom they represent or by any other Trading Participants.

(e) Borrowing money or securities from clients in connection with any transaction in securities.

(f) Dividing or otherwise splitting commissions, profits or other compensation in connection with the purchase or sale of securities with any other person not licensed as a trader or salesman.

(g) For traders and salesmen who have information that a client has placed a buy or sell order, from buying or selling in the same way, including buy or sell orders made for discretionary account, until the

client's order or decision to buy or sell has been executed or canceled. However, this prohibition shall not include cases where there is an expressed order to trade from the client owning the discretionary account.

(h) Taking advantage, directly or indirectly, of any material non-public information pertaining to a security and/or to a Trading Participant such as, but not limited to, unpublished research material and/or a firm's shareholdings. Traders and salesmen shall ensure that no person, including their relatives within the fourth degree of affinity or consanguinity, shall, directly, take hold of, have access to, or take advantage of such material non-public information.

(i) When allocating securities traded in the Exchange, from apportioning said securities among themselves without having first satisfied to the extent possible all client orders.

(j) Undertaking any transaction or engaging in any other work which reduces their contribution or efficiency in their duties and responsibilities to their company and clients.

Section 7. *Bribery.* (a) A trader or salesman shall not accept or solicit an advantage from any person in connection with his company's business if such act can influence his objectivity in performing his duties, induce him to act against the interest of his company and clients, or lead to allegations of impropriety.

(b) A trader or salesman shall not offer an advantage to any person or entity for the purpose of influencing such person or entity in relation to any business dealings.

Section 8. *Confidentiality.* Traders and salesmen may come across non-public or confidential information on listed companies or their clients or employer. Without prejudice to the disclosure and other requirements of the Securities Laws or other relevant laws, traders and salesmen have a fiduciary duty in respect of such information and, unless authorized by the relevant parties, shall not disclose, share or otherwise use the information, especially for their personal gain or benefit.

Section 9. *Market Rumors.* Traders and salesmen shall not initiate or otherwise participate in market rumors, which may lead to allegations of price manipulation or insider trading.

Section 10. *Gambling.* Traders and salesmen shall not engage in excessive gambling of any kind with persons having business dealings with their company. In social games of chance with clients or business associates, they must exercise judgment and withdraw from any high stake games.

Section 11. *Responsibilities of Trading Participants.* Trading Participants shall have the following responsibilities:

(a) Trading Participants shall ensure that their Associated Person or any person designated to perform his function ensure that appropriate internal procedures are in place to implement Section 4 above with respect to traders' and salesmen's trading for their own account. The written consent of such Officers shall state the following information:

(i) Any restriction or condition that the concerned Trading Participant may deem appropriate and necessary to impose;

(ii) The date and time when the consent was given;

(iii) The duration of the validity of such written consent. The written approval shall be valid until otherwise revoked; and

(iv) The signature of the officer attesting to the truth and accuracy of the foregoing information.

(b) Trading Participants shall determine whether traders and salesmen shall be allowed to participate in:

(i) Placements handled by the firm; and

(ii) Initial Public Offerings (IPOs)

(c) Trading Participants shall prepare and maintain the ledgers of traders and salesmen who deal for their own accounts and those ledgers should be made readily available to CMIC or the Commission whenever requested. Furthermore, copies of pertinent supporting documents to traders' or salesmen's transactions such as, but not limited to, order tickets, confirmation vouchers, in-receipts, out-receipts, credit and debit memos, corresponding checks as payments for a purchase and as proceeds for a sale, should be maintained but need not be attached to the ledger. In the case of order tickets, copies may either be hard copies or any copy in electronic format.

(d) Trading Participants should also establish appropriate procedures, guidelines and mechanics to monitor and control personal transactions of traders and salesmen to see to it that the privilege granted to traders and salesmen to trade for their own accounts is not abused. **Established procedures, guidelines and mechanics should include provision for review and approval of individual transactions by the Associated Person.**

(e) Trading Participants should adopt these rules as part of their internal control system and ensure that the provisions thereof are fully complied with by their traders and salesmen, and Associated Person.

Section 12. *Relationship of Trading Participants with CMIC.* Trading Participants and their directors, officers, employees and duly authorized agents shall exercise utmost professionalism in dealing with CMIC.

The Trading Participants and their representatives shall be held liable for any unprofessional behavior or conduct towards any member, employee or duly authorized agent of CMIC, such as but not limited to the following:

- (a) Physical harm or acts that cause or may likely cause mental or emotional suffering, such as, intimidation, harassment, damage to property, public ridicule, humiliation, verbal abuse and threats of such acts;
- (b) Offer of money or other valuable consideration;
- (c) Non-cooperation in providing the required documents and/or information; and
- (d) Any other act unbecoming of a securities market professional.

Section 13. *Mandatory Compliance with the Provisions.* In order to attain the objectives of the foregoing code of conduct, Trading Participants and all licensed traders and salesmen employed by Trading Participants are enjoined to strictly observe the provisions thereof.

ARTICLE VI. CONDUCT REGULATION OF TRADING PARTICIPANTS

Section 1. *Ethical Standards Rule.* (a) Every Trading Participant and Associated Person and salesman of a Trading Participant (hereinafter referred to as a "Registered Person"), in the conduct of his business, shall observe high standards of commercial honor and just and equitable principles of trade.

(b) In considering whether a Registered Person is conducting his business in an ethical and fair manner, CMIC, in addition to requirements imposed under other SRC Rules, will be guided by the following principles and requirements which incorporate International Organization of Securities Commission standards.

(i) **Honesty and fairness.** In conducting his business activities, a Registered Person should act honestly, fairly and in the best interest of his client and for the integrity of the market.

Where a Registered Person advises or acts on behalf of a client, he shall ensure at all times that any representations or other communications made and information provided to the client are accurate and not misleading and do not violate SRC Rule 24.1 (d), paragraph 1.

(ii) **Diligence.** In conducting his business activities, a Registered Person should act with due skill, care and diligence, in the best interest of his clients and for the integrity of the market.

(a) A Registered Person shall take all reasonable steps to promptly execute client orders and in conformity with the instruction of the client.

(b) A Registered Person when acting for or with a client shall always execute client orders on the best available terms in compliance with SRC Rule 32.2 (a).

(c) A Registered Person 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.

(d) When providing advice to a client, a Registered Person shall act diligently and ensure that his advice and recommendations in relation to clients are based on thorough analysis and take into account available alternatives.

(iii) **Capabilities.** A Registered Person should have and employ effectively the resources and procedures which are needed for the proper performance of his business activities.

(a) A Registered Person shall ensure at all times that any person he employs or appoints to conduct business for or with clients or other registered persons is qualified, including having relevant training or experience to act in the capacity so employed or appointed in compliance with SRC Rules 28.1, paragraph 4 and 28.2.

(b) A Registered Person shall ensure that at all times, pursuant to SRC Rule 30.2, paragraph 7, he has:

(1) Adequate resources to diligently supervise and does diligently supervise his employees and all persons appointed by him to conduct business for or with clients or any other registered persons; and

(2) Satisfactory internal control procedures and financial and operational capabilities which can be reasonably expected to protect his operations, his clients and other registered persons from financial loss arising from the theft, fraud and other dishonest acts, or professional misconduct or omissions of all company officers, employees and authorized representatives.

(iv) Information about clients.

(a) A Registered Person should seek from his clients, information about their financial situation, investment experience and investment objectives relative to the services to be provided pursuant to SRC Rule 52.1, paragraph 6 and other applicable laws. Should a client refuse to divulge his exact financial condition, the Trading Participant can provide an estimate thereof to comply with the requirements of the Anti-Money Laundering Law and its implementing rules and regulations

(b) A Registered Person shall take all reasonable steps to establish the true and full identity of each of his clients, their financial situation, investment experience, and investment objectives.

(c) Having regard to information disclosed by a client and other circumstances relating to the client which the Registered Person is or should be aware of through the exercise of due diligence, the Registered Person shall ensure that such recommendation or solicitation for that client is reasonable and suitable in all circumstances pursuant to SRC Rule 30.2, paragraph 4.

(d) A Registered Person providing services to any client, in relation to derivatives, including options and warrants, or any leveraged transaction, shall assure himself that the client understands the nature and risks of these instruments and has sufficient net worth to be able to

assume the risks and bear the potential losses of trading in such instruments.

(e) A Registered Person should be reasonably satisfied about the identity, address and contact details of the person ultimately responsible for originating the instruction in relation to a transaction, the person who stands to gain the commercial or economic benefit of the transaction and/or bears the commercial or economic risk; *provided, however*, that in relation to an investment company, or discretionary account, the person referred to above is the investment company or account, not those who hold a beneficial interest therein.

(f) A Registered Person shall keep in the Philippines a record of the details referred to above and provide **CMIC** with access to those records upon request pursuant to Section 52 of the Code and SRC Rule 52.1, paragraph 1.

(g) A Registered Person shall not do anything to effect a transaction unless he has first complied with the requirements of this rule, as required in SRC Rule 30.2, paragraph 4.

(v) Information for clients. A Registered Person shall make adequate disclosure of material information in his dealings with his clients.

(a) A Registered Person shall ensure that a written agreement which complies with SRC Rule 30.2, paragraph 3 is entered into with a client before any services are provided to that client.

(b) A Registered Person shall provide clients with adequate information about his firm, including his business address, any relevant conditions or restrictions under which the Registered Person conducts his business, and the identity or status of employees and others acting on his behalf with whom the client may have contact.

(c) After a Registered Person has effected a transaction for a client, he shall endeavor to confirm promptly with the client, in writing, the essential features of the transaction pursuant to SRC Rule 30.2.

(d) A Registered Person shall comply with SRC Rule 52.1, paragraph 8, regarding customer account statements.

(e) A Registered Person shall disclose the financial condition of his business to a client upon request by providing a copy of the most recent report required to be filed with **CMIC and/or** the Exchange under SRC Rule 52.1, paragraph 5 (Audited Financial Statements) and SRC Rule 49.1 paragraph 1 (A) (iii) (Net Capital) and disclose any material changes which adversely affect the Registered Person's financial condition after the date of such filing.

(vi) Conflicts of Interest. A Registered Person should avoid conflicts of interest and when they cannot be avoided, should ensure that his clients are fairly treated and properly informed of such conflicts of interest.

(a) Client priority - A Registered Person shall handle orders of clients fairly and in the order in which they are received in compliance with SRC Rule 34.1, paragraph 1.

(1) Orders of clients, or transactions to be undertaken on behalf of clients, shall have, in all cases, priority over orders for the account of the Registered Person, and otherwise comply with SRC Rule 34.1, paragraph 1 where the Trading Participant is a Member of an Exchange;

(2) A Registered Person shall, where he has aggregated an order for a client with an order for another client, or with an order for his own account, give priority to satisfying orders of clients, in any subsequent allocation, if all orders cannot be filled;

(3) A Registered Person shall not deal in any securities for himself or for any account in which he has an interest based upon advanced knowledge he possesses of pending transactions for or with clients or any other nonpublic information, the disclosure of which would be expected to affect the price of such securities and violate Section 27 of the Code (insider trading prohibition);

(4) A Registered Person who withdraws in whole or in part from providing any investment or related service shall ensure that affected clients are promptly notified of such action and that any business which remains outstanding is promptly completed or transferred to another registered person in accordance with SRC Rule 29 and any instruction of the affected clients.

(b) Conflicts of interest - Where a Registered Person has a material interest in a transaction with or for a client, or a relationship which gives rise to an actual or potential conflict of interest in relation to such transaction, he shall neither advise, nor deal in relation to the transaction unless he has disclosed that material interest or conflict to the client and has taken all reasonable steps to ensure fair treatment of the client.

(c) Client assets - A Registered Person shall, in the handling of client transactions and assets, act to ensure that client assets are accounted for properly and promptly and comply with SRC Rule 52.1, paragraph 10. Where the Registered Person, or a third party on behalf of the Registered Person, is in possession or control of client positions or assets, the Registered Person shall ensure that client positions or assets are adequately safeguarded.

(vii) Compliance - A Registered Person shall comply with all regulatory requirements applicable to the conduct of his business activities so as to promote the best interest of clients and the integrity of the market.

(a) A Registered Person shall comply with the Code, rules and regulations adopted thereunder, and rules of **CMIC**, the Exchange, the Clearing Agency, or other SRO, of which he is a member of or participant in.

(b) A Registered Person shall have a policy, which has been communicated to employees in writing, on whether employees are permitted to deal for their own accounts in securities. If employees are permitted to deal, the conditions on which they may do so, including those imposed under SRC Rule 34.1, paragraph 1, shall be set out in writing and communicated to each employee.

(c) A Registered Person shall ensure that complaints from clients relating to his business are adequately addressed in compliance with SRC Rule 30.2, paragraph 6 (B) (vii) and sufficient records of such complaints are made in compliance with SRC Rule 52.1, paragraph 9.

(d) A Registered Person shall at all times be responsible for the acts or omissions of his employees and agents in respect to the conduct of his business, pursuant to Section 51 of the Code.

(e) All Registered Persons, as a condition of their registration, shall undertake in writing to uphold the Code, and rules and regulations adopted thereunder.

(c) This rule applies to all Registered Persons, although CMIC recognizes that certain requirements of the Code and rules adopted thereunder may not be within the control of an Associated Person. In considering the conduct of an associated person, CMIC will consider such person's level of responsibility within the Trading Participant, and the level of control or knowledge he may have considering any failure by his firm or persons under his supervision to follow the Code.

(d) Where CMIC makes an inquiry under Sec. 53 of the Code, CMIC will refer to the requirements set forth in this Rule in considering whether any person is guilty of a violation of the Code and should remain registered.

Section 2. Supervision. (a) The management of every Trading Participant shall establish and maintain an appropriate and effective compliance function within the firm which is independent of all operational and business functions. The compliance function shall be performed by an Associated Person who shall be registered with the Commission and required to report directly to the board of directors and the company President. The management shall ensure that the Associated Person/s performing the compliance function possesses sufficient training and experience in securities regulation

matters and an understanding of the securities activities of the firm enabling them to effectively execute their duties.

(b) Associated Persons shall be responsible, in addition to the duties enumerated under SRC Rule 28.1 (4) (G) for maintaining a system to supervise the activities of all persons employed by the Trading Participant who are directly or indirectly related to the conduct of its securities business. The supervisory system shall be reasonably designed to achieve compliance with the rules of CMIC, other applicable laws, including, but not limited to, Republic Act No. 9160, as amended, or the Anti-Money Laundering Act (“AMLA”), and the Trading Participant’s own internal policies and procedures. A firm’s supervisory system shall include at least the following:

(i) establishment and maintenance of written supervisory procedures, including procedures for establishing and maintaining a “Chinese Wall,” taking into consideration the applicable requirements under AMLA and the Code of Corporate Governance;

(ii) designation of one or more Associated Persons with the authority and responsibility to carry out the supervision of each type of business in which it engages;

(iii) titles, registration status and locations of the required Associated Person/s and the responsibilities of each Associated Person as these relate to the types of business engaged in;

(iv) written documentation to prove that all Associated Persons are qualified by virtue of experience or training to carry out their assigned supervisory responsibilities;

(v) written documentation to prove that each person engaged in securities transactions, either collectively or individually, has participated no less than annually in an interview or meeting conducted by the Associated Person/s designated by the firm at which compliance matters relevant to the activities of these persons are discussed. There shall be prompt notification in writing to each such person of new or modified compliance obligations;

(vi) establishment of an effective management and organizational structure which ensures that the operations of the business are conducted in a sound, efficient and effective manner;

(vii) establishment, maintenance and enforcement of policies and procedures to ensure the proper handling of complaints from clients and that appropriate remedial action is promptly taken. Where possible, complaints should be investigated by the Associated Person performing the compliance function who is not directly involved in the subject matter of the complaint. Where a complaint is not remedied promptly, the client shall be advised of any further steps which may be available to the client under the law; and

(viii) establishment of policies and guidelines to comply with the requirements of the AMLA.

(c) Although final responsibility for proper supervision shall rest with the Trading Participant, diligence of a good father of the family is required from the Associated Person/s in the conduct of their compliance function.

(d) Associated Person/s shall promptly report to management all occurrences of material non-compliance by the firm or its staff with legal and regulatory requirements, as well as with the firm's own policies and procedures. Management shall then promptly notify CMIC. For this purpose, the Associated Person must maintain a logbook of all material non-compliance reports with the appropriate notation of the action taken by management on the said occurrences. Such logbook must be duly registered with the Commission within fifteen (15) days from issuance of the Associated Person/s new/renewal license.

(e) Notwithstanding the requirement in the immediately preceding paragraph, all Associated Persons must prepare, sign and file with CMIC not later than fifteen (15) days after the end of each calendar quarter, a Compliance Report on the firm's compliance and/or non-compliance with the provisions of the Code and its implementing rules and regulations including, but not limited to, the following concerns:

- (i) whether the firm complies with the requirements of the Code and the implementing rules;
- (ii) the significant findings of non-compliance; and
- (iii) information on the action taken by management to address the issue.

The said report shall also include a summary of all occurrences of material non-compliance by the Trading Participant or its staff, salesmen and other agents with legal and regulatory requirements and the actions taken by management on such violations.

(f) Further, Trading Participants should comply with the provisions on (1) Done Through Transactions; (2) Non-Exchange Transactions; and (3) Non-Exchange Trades Involving Change in Beneficial Owner contained in the Trading Rules of the Exchange.

Section 3. *Internal or Accredited Training Program.* (a) Every Trading Participant shall establish, implement and maintain a reasonably comprehensive system of training towards –

- (i) ensuring the continuing improvement in critical areas of its principal activities and operations; and
- (ii) enhancing the technical knowledge of its employees to enable them

to understand the operational and internal control policies and procedures of that Trading Participant and all applicable legal and regulatory requirements.

(b) Such system of training shall be properly documented in a manual which shall:

(i) set out details of the training programs that the Trading Participant proposes to implement; and

(ii) be regularly updated in line with the development in the securities industry.

(c) All Trading Participants shall submit to CMIC **no later than the 29th of January of each year** a yearly schedule/timetable of the implementation of its training program. At a minimum, such report should contain the following information:

(i) The implementation of the previous year's internal training program with details on seminar dates, number of participants, and other pertinent information; and

(ii) Current year's seminar topics (with description), projected dates, target market, and planned speaker.

(d) The Trading Participant may, at its option, substitute its internal training program submitted at the time of renewal of its license by enrolling in training programs sponsored by associations or organizations duly accredited or recognized by the Commission, provided, however, that proper approval is obtained from the Commission on such substitution. It is the responsibility of Trading Participants, through its Associated Person, to provide periodic training to its officers and employees whether externally or internally, the occurrence of which shall not be dependent solely on the expectation that an external seminar will be sponsored at a later time.

Section 4. Submission of Names of Stockholders, Members, Participants, Clients and Related Information. Every Trading Participant required to register under the Code shall immediately report to CMIC and any person deputized and/or duly authorized by CMIC pursuant to Section 5(h) of the Code, the names of their owners/stockholders, members, participants, and clients, and other related information in its or his possession, upon order of CMIC, in pursuance of an investigation, examination, official inquiry or as part of a surveillance procedures, and/or in compliance with other pertinent laws.

Section 5. Advertisement and Communications with the Public. (a) All communications by Trading Participants or Associated Persons or salesmen of Trading Participants, with the public shall be based on principles of fair dealing and good faith and should provide a sound basis for evaluating the facts in regard to any particular security or securities or type of security, industry discussed, or service offered. No material fact or qualification may be omitted if the omission, in the light of the context of the material presented, would cause the advertising or sales literature to be misleading.

(b) Exaggerated, unwarranted or misleading statements or claims are prohibited in all public communications of Registered Persons. In preparing such literature, it must be borne in mind by Registered Persons that inherent in investment are the risks of fluctuating prices and the uncertainty of dividends, rates of return and yield, and no Registered Person shall, directly or indirectly, publish, circulate or distribute any public communication that he knows, or had reason to know, contains any untrue statement of a material fact or is otherwise false or misleading.

(c) Communications with the public shall not contain promises of specific results, exaggerated or unwarranted claims or unwarranted superlatives, opinions for which there is no reasonable basis, or forecasts of future events which are unwarranted, or which are not clearly labeled as forecasts.

In judging whether a communication or a particular element of a communication may be misleading, several factors should be considered, including but not limited to:

(i) The overall context in which the statement or statements are made. A statement made in one context may be misleading even though such a statement could be perfectly appropriate in another context. An essential test in this regard is the balance of treatment of risks and potential benefits.

(ii) The audience to which the communication is directed. Different levels of explanation or detail may be necessary depending on the audience to which a communication is directed and the ability of the Registered Person given the nature of the media used, to restrict the audience appropriately. If the statements made in a communication would be applicable only to a limited audience, or if additional information might be necessary for other audiences, it should be kept in mind that it is not always possible to restrict the readership of a particular communication; and/or

(iii) The clarity of the communication. A statement or disclosure made in an unclear manner can result in a failure to understand the statement, or in a serious misunderstanding. A complex or overly technical explanation may cause even greater misunderstanding than too scant information. Likewise material disclosure relegated to legends or footnotes may not generally enhance the reader's understanding of the communication.

Section 6. *Publication of Transactions and Quotations.* No Trading Participant, or Associated Person or salesman of a Trading Participant, shall publish or circulate, or cause to be published or circulated, any notice, circular, advertisement, newspaper article, investment service, or communication of any kind which purports to report any transaction as a purchase or sale of any security unless such person believes that such transaction was a bona fide purchase or sale of such security; or which purports to quote the bid price or asked price for any security, unless such person believes that such quotation represents a bona fide bid for, or offer of, such security.

Section 7. *Suitability Rule.* In recommending to a customer the purchase,

sale or exchange of any security, a Trading Participant or an Associated Person or salesman of a Trading Participant, shall have reasonable grounds for believing that the recommendation is suitable for such customer upon the basis of the facts disclosed by such customer as to his other security holdings and as to his financial situation and needs.

Except as provided in SRC Rule 52.1, paragraph 6, prior to the execution of a transaction recommended to a customer, a Trading Participant shall execute a customer account information form which complies with SRC Rule 52.1, paragraph 6.

Section 8. *Prohibition on Guarantees.* No Trading Participant or salesman shall guarantee against loss in any securities account of such customer carried by the Trading Participant or in any securities transactions effected by the Trading Participant with or for the customer.

It shall be unlawful for any Trading Participant of the Exchange, directly or indirectly, to endorse or guarantee the performance of any security registered with the Commission and/or listed on the Exchange.

Section 9. *Payment to Influence Market Price.* No Trading Participant shall, directly or indirectly, give, permit to be given, or offer to give, anything of value to any person for the purpose of influencing or rewarding the action of such person in connection with the publication or circulation in any newspaper, investment service, or similar publication, of any matter which has, or is intended to have, an effect upon the market price of any security, provided that this rule shall not be construed to apply to a matter which is clearly identifiable as paid advertising.

Section 10. *Commissions and Charges for Services Performed by a Trading Participant.* (a) Charges by a Trading Participant for services performed, including:

- i. miscellaneous services such as collection of monies due for principal, dividends or interest;
- ii. exchange or transfer of securities; and
- iii. appraisals, safekeeping or custody of securities, and other services,

shall be reasonable.

(b) CMIC, when it deems necessary to enforce the Securities Laws, may require a Trading Participant to disclose in writing to CMIC its commission or remuneration in a particular transaction.

ARTICLE VII. CUSTOMER PROTECTION

Section 1. *Customer Account Information Rule.* Every Trading Participant shall maintain customer accounts opened as follows:

- (a) For each account, the following information:
 - (i) Customer's name, residence address and residence telephone, and e-mail address, if any;
 - (ii) Date and place of birth;
 - (iii) Whether customer is an institutional customer;
 - (iv) Nationality;
 - (v) Signature of the salesman introducing the account and signature of the partner, officer or manager who accepts the account;
 - (vi) If the customer is a corporation, partnership or other legal entity, the names of any person authorized to transact business on behalf of the entity;
 - (vii) Specimen signature; and
 - (viii) Option whether confirmation of customer orders would be via courier or electronically.
- (b) For each account other than an institutional account, the Trading Participant shall obtain, prior to the settlement of the initial transaction in the account, the following information **and/or documents** to the extent it is applicable to the account:
 - (i) Customer's tax identification number;
 - (ii) Occupation of customer and name and address and telephone number of employer, and e-mail address, if employed;
 - (iii) Whether the customer is employed by or otherwise associated with another Trading Participant (e.g., officer, director, salesman, or shareholder);
 - (iv) Whether the customer is an officer or director of a company listed on an exchange;
 - (v) The customer's investment objective and other related information concerning the customer's financial situation and needs;

(vi) If duplicate confirmations are required to be sent to another person, the identity of that person and his relationship to the customer; and

(vii) Source of funds **and proof of financial capacity such as, but not limited to, bank certificate/s, income tax return, professional license, and/or business permit.**

(c) For discretionary accounts, the Trading Participant shall also:

(i) Obtain the signature of each person authorized to exercise discretion in the account; and

(ii) Record the date such discretion is granted.

(d) For corporate or institutional accounts, the Trading Participant shall obtain, prior to the settlement of the initial transaction in the account, the following information **and/or documents** to the extent it is applicable to the account:

(i) Articles of Incorporation/Partnership;

(ii) By-laws;

(iii) Official address or principal business address;

(iv) Secretary's certificate of board resolution authorizing the opening of the account with the Trading Participant;

(v) List of directors/partners;

(vi) List of stockholders owning at least two percent (2%) of the capital stock;

(vii) Contact numbers;

(viii) Beneficial owners, if any;

(ix) Verification of the authority and identification of the person purporting to act on behalf of the client;

(x) Financial Information;

(xi) Investment objective; and

(xii) All other information contained in the prescribed Customer Account Information Form ("CAIF").

(e) If more than one party is named on the account, new account information shall be obtained for each party on the account.

(f) If the account is a trust account, a copy of the trust agreement shall be obtained. The agreement shall specify the types of transactions that the trustee is allowed to perform. These accounts cannot be margin accounts unless specifically authorized by the trust agreement.

(g) A Trading Participant may maintain a numbered account for a client who wishes to keep his name confidential. If numbered accounts are used, the firm shall keep on file (i) the name of the customer and (ii) a written statement signed by the customer showing that the customer owns the account.

(h) The Trading Participant shall develop clear customer acceptance policies and procedures when conducting business relations or accommodating specific transactions and shall exercise due diligence in implementing its policies and procedures. Furthermore, it shall adopt adequate internal control measures for verifying and recording the true and full identify of their customers. It shall require customers to produce original documents of identity issued by an official authority, preferably bearing a photograph of the customer and where practicable, maintain file copies of documents of identity; otherwise, relevant details on the identity documents will be recorded.

(i) In the case of corporate clients, the Trading Participant shall 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 and shall exercise due diligence in implementing its policies and procedures. It shall endeavor to ensure, prior to establishing business relationships, that the corporate entity has not been or is not in the process of being dissolved, wound up, liquidated, or voided, or that its business or operation 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.

(j) In addition to the requirements prescribed in the immediately preceding paragraphs, in the case of customers who are acting as trustee, nominee, agent or in any capacity for and on behalf of another, the Trading Participant shall verify and record the true and full identity of the person(s) on whose behalf a transaction is being conducted. In case of doubt as to whether such persons are being used as dummies in circumvention of existing laws, the firm shall immediately make the necessary inquiries to verify the status of the business relationship between the parties.

(k) Anonymous accounts, accounts under fictitious names, and all other similar accounts shall be absolutely prohibited.

(l) Numbered accounts are allowed for trading purposes provided that the owner fills up the CAIF with his identity clearly indicated in the form or the owner is otherwise identified in accordance with Sec. 1 (g), Article VII.

(m) The Trading Participant cannot create new accounts without a face-to-face meeting.

(n) All existing CAIFs of active clients shall be updated or amended annually to comply with the new requirements within the period prescribed in the SRC Rules.

(o) **All CAIFs shall include a certification by the Trading Participant that the latter checked the CAIF and found the same to be complete in form and substance, with all relevant supporting documents attached thereto, and that any representations made by the client in the CAIF was confirmed by the Trading Participant with the client in accordance with the Know-Your-Client or KYC provisions of the Anti-Money Laundering Act (“AMLA”).**

(p) It is the Trading Participant’s duty to know its clients well and, accordingly, it shall be primarily responsible in keeping current all material information contained in the CAIF.

(q) The Trading Participant, its directors, officers, and Associated Persons are required to report any suspicious client transaction to the Anti-Money Laundering Council (“AMLC”), pursuant to the provisions of the AMLA.

For purposes of this section, a “suspicious client transaction” shall mean any transaction which causes any ordinary person to have a feeling of apprehension or mistrust about the transaction considering (a) its unusual nature or circumstances, or (b) the person or group of persons with whom they are dealing, and based on the bringing together of all relevant factors including knowledge or the person’s or persons’ business or background (as well as behavioral factors).

(r) Trading Participants should also comply with the provisions on Identification of Customers’ Accounts and Orders through the Use of Code, Symbol or Account Number and Multiple Accounts contained in the Trading Rules of the Exchange.

Section 2. *Client Agreement.* (a) A Trading Participant and its Registered Persons who deal directly with clients shall ensure that a written agreement (the “Client Agreement”) is entered into with a client before any service is provided to that client.

(b) The Client Agreement shall be in a language understood by the client. The Registered Persons who deal directly with clients shall explain to the client the contents of the agreement.

(c) A Client Agreement shall contain, among others, the following information:

i. the full name and address of the client, as evidenced by a retained copy of the identity card, relevant sections of the passport, business registration certificate, corporation documents, or any other official document which uniquely identifies the client;

- ii. the full name and registered address of the Trading Participant;
- iii. the Trading Participant's registration status with the Commission;
- iv. undertakings by the Trading Participant and the client to notify the other in the event of any material change to the information provided in the agreement;
- v. a description of the nature of services to be provided to or available to the client, such as securities cash account, securities margin account, discretionary account, portfolio management, investment advice, and derivatives trading;
- vi. a description of any remuneration (and the basis for payment) that is to be paid by the client to the Trading Participant, such as commission, brokerage, and any other fees and charges;
- vii. a statement indicating the circumstances under which the Trading Participant will be acting as principal in relation to the client and that in all other circumstances the Trading Participant will be acting as agent for the client;
- viii. if the Trading Participant is acting as a Dealer in relation to securities and is an Exchange Trading Participant, a statement explaining the application of Section 34 of the Code, and if the client specifically authorizes the Dealer to pledge the client's securities or subject such securities to liens of third parties;
- ix. if margin or short selling facilities are to be provided to the client, details of margin requirements, interests charges, margin calls, and the circumstances under which a client's position may be closed without the client's consent; and
- x. risk disclosure statement as set forth in Annex 30.2-A of the SRC.

(d) A Registered Person shall ensure that he complies with his obligations under this rule and the Client Agreement and that the Client Agreement does not operate to remove, exclude, or restrict any rights of a client or obligations of a Trading Participant under the Code.

(e) A Trading Participant shall not effect a transaction on behalf of a client unless, before the transaction is effected, the client, or a person designated by the client, specifically authorizes the transaction, or the client has authorized in writing the Trading Participant to effect transactions on behalf of the client without the client's specific authorization. If the Trading Participant has obtained such an authorization, the Client Agreement shall specify that the account is a discretionary account.

(f) A copy of the required Client Agreement is set forth in Annex 30.2-B of the SRC Rules.

Section 3. *Discretionary Accounts.* (a) Discretionary Accounts shall be classified as either a General Discretionary Account or a Specific Discretionary Account. In a General Discretionary Account, the customer and the Trading Participant agree in writing that the Trading Participant can effect transactions on behalf of the customer without need of obtaining the customer's specific authorization and instructions for each transaction. In a Specific Discretionary Account, the customer and the Trading Participant agree in writing that the Trading Participant shall have discretionary authority to effect on behalf of the client only the specifically authorized transaction.

(b) The Trading Participant shall periodically review the transactions of the Discretionary Account as may be reasonably necessary to detect and prevent transactions, which are excessive in value or frequency considering the financial resources and character of the account and the agreement between the Trading Participant and the customer.

(c) No Trading Participant shall effect, for and on behalf of a Discretionary Account, any transaction, which is excessive in value or frequency considering the financial resources and character of the account and the agreement between the Trading Participant and the customer.

(d) A Trading Participant with discretionary authority to determine, for and on behalf of a customer, (i) whether the transaction shall be a purchase or sale or (ii) the security and/or the amount thereof to be bought or sold, may:

(i) Effect a transaction for or with such customer in any security in which the Trading Participant has a long or short position, or in the distribution or accumulation of which it has any direct financial interest, or in which it holds, or has granted or has knowledge that any of its principals holds or has granted any option, provided that the Trading Participant discloses to the customer such position, interest or option and obtains the written consent of the customer to the transaction; or

(ii) Buy from or sell to such customer any security for any account in which the Trading Participant or any of its principals has an interest, provided that the Trading Participant discloses such interest to the customer and obtains the written consent of the customer to the transaction.

Section 4. *Order Ticket Rule.* (a) Every order received by a Trading Participant or any other Associated Person or salesman of a Trading Participant to buy or sell securities for customers shall be entered on an order form, which shall contain at the minimum, all the information required by this Rule. Each buying or selling order form shall be time stamped by the Trading Participant or any other associated person or salesman of a Trading Participant or any person acting on his behalf upon receipt of the customer's order and upon transmission to the trading floor, if necessary. Time recording of subsequent action on an order, whether for amendment, cancellation or actual matching thereof, shall be captured by the computerized trading system of the Exchange or by time stamping, for over-the-counter transaction. Any such information

captured by the computerized trading system of the Exchange shall be printed and made available for legal and/or audit purposes.

(b) All the necessary time recordings shall be disclosed for confirmation to the customer upon his request.

(c) All Trading Participants, who deal for their own account either directly or where a Trading Participant, through another Trading Participant, or trade for a discretionary account, as well as their partners, floor traders, officials and employees, shall record all purchase and sale orders on the same order form used by such Trading Participants for their customers, and such order forms shall also be time-stamped as required by paragraph (a) above.

(d) Every Trading Participant, Associated Person and salesman of a Trading Participant, executing an order for a transaction in securities shall enter on the order ticket whether the transaction will be matched through the Exchange trading system or transacted as a block sale, in accordance with SRC Rule 30.2, paragraph 8, whether the firm is acting as agent or principal in connection with the transaction; *provided, however*, Trading Participants are required to comply with SRC Rule 34.1, paragraph 1 when placing orders for their own account.

(e) The order ticket shall reflect the terms and conditions of the order or instructions, including a notation if the order is a short sale, and any subsequent modification or cancellation, the name of the customer for which the order was entered, the name of the salesman who took the order, the price at which it is executed, and whether the order was solicited or unsolicited.

(f) The designation should be entered on real time on the order ticket and indicated on the confirmation.

(g) All purchase and sale orders for the same security and under the same terms and conditions, including those placed by the Trading Participant for its own account or for discretionary accounts and those placed by partners, floor traders, officials and employees, shall be executed by the Trading Participant in the order in which they were received; *provided, however*, Trading Participants shall comply with SRC Rule 34.1, paragraph 1 regarding priority of customer orders.

(h) All time stamping machines that are being used by Trading Participants for the purposes of this Rule should be synchronized at all times in accordance with the official time of the Exchange and time stamping prints should always be clear.

(i) A Trading Participant may seek exemption from the paper format requirements of this Rule and instead apply for an electronic format. Such application has to be approved by the Commission.

Section 5. *Purchases and Sales in Cash Account.* (a) Purchases by a customer in a cash account shall be paid in full within three (3) business days after the trade date.

(b) If full payment is not received within the required period, the Trading Participant shall cancel or otherwise liquidate the transaction, or the unsettled portion thereof, starting on the next business day but not beyond ten (10) business days following the last day for the customer to pay, unless such sale cannot be effected within said period for justifiable reasons.

(c) If a transaction is cancelled or otherwise liquidated as a result of non-payment by the customer, prior to any subsequent purchase during the next ninety (90) days, the customer shall be required to deposit sufficient funds in the account to cover each purchase transaction prior to execution.

(d) If the amount of money due from a customer in a cash account is less than *Ten Thousand Pesos (P10,000.00)*, the Trading Participant may choose not to take the action required by paragraph (b).

(e) Exceptions to paragraphs (a), (b), and (c) include instances when the security purchased is unissued or where the purchase is made by the customer with the understanding that payment is to be made upon delivery.

(f) If a Trading Participant executes a sell order of a customer (other than an order to execute a sale of securities which the seller does not own) and if for any reason whatsoever the Trading Participant has not obtained possession of the securities from the customer on the next business day after settlement date but not beyond ten (10) business days for the customer to deliver the securities, the Trading Participant shall immediately thereafter close the transaction with the customer by purchasing securities of like kind and quantity, unless such purchase cannot be effected within said period for justifiable reasons.

(g) If the Trading Participant is required to take the action required by paragraph (f), prior to any subsequent sale during the next ninety (90) days, the customer will be required to place the securities on deposit in the account prior to execution of the transaction.

Section 6. *Margin.* A Trading Participant shall not extend credit to a customer in an amount that exceeds fifty percent (50%) of the current market value of the security at the time of the transaction. In no event shall new or additional credit be extended in an account in which the equity is less than P50,000.00.

The margin maintained in a margin account of a customer shall be no less than twenty five percent (25%) of the current market value of all securities "long" in the account and thirty percent (30%) of the current market value of securities "short" in the account.

Section 7. *Call for Additional Margin.* When there is an insufficiency of margin, a call for additional margin shall be issued promptly by the Trading Participant to the customer. A call for initial margin shall be satisfied within five (5) business days

from the date the insufficiency is created. A call for maintenance margin shall be satisfied within twenty-four (24) hours after the call is issued.

Section 8. *When Call for Additional Margin Not Met.* If a margin call is not met within the time prescribed in paragraph (7) above, the Trading Participant shall liquidate securities sufficient to meet the margin call or eliminate the margin deficiency existing on the day such liquidation is required, whichever is less. The Trading Participant shall liquidate the securities through the Exchange or in the best available public market. If the margin deficiency in the account is less than P10,000, no action need be taken by the Trading Participant.

Section 9. *Extension of Margin Call Period.* The required payment date for a call for initial margin may be extended by seven (7) days upon written application delivered by hand or facsimile transmission by the Trading Participant to **CMIC**. In granting such an extension, **CMIC** will take into consideration whether the Trading Participant and the customer are acting in good faith and whether exceptional circumstances warrant such extension. Application for the extension must be received and acted upon before the expiration of the original payment period or the expiration of any previous extension.

Section 10. *Regulation of Short Sale.* Short selling transactions shall be governed by these rules and the revised Rules on Short Selling and implementing guidelines. (a) Calculation. The Trading Participant shall calculate, as of 15th day and as of the last day of each calendar month, the aggregate short position of each individual account in respect of each security.

(b) Written Report. The Trading Participant shall file a written report of the calculation of the short position to CMIC within two (2) days following the date of computation.

(c) Definition. The term "short sale" shall mean any sale of a security which the seller does not own or any sale which is consummated by the delivery of a security borrowed by, or for the account of the seller.

A person shall be deemed to own a security if:

- (i) he or his agent has title to it;
- (ii) he has purchased, or has entered into an unconditional contract, binding on both parties thereto, to purchase it and has not yet received it;
- (iii) he owns a security convertible into or exchangeable for it and has tendered such security for conversion or exchange;
- (iv) he has an option to purchase or acquire it and has exercised such option; or

(v) he has rights or warrants to subscribe to it and has exercised such rights or warrants provided, however, that a person shall be deemed to own securities only to the extent he has a net long position in such securities.

(d) Determination of Good Delivery. No Trading Participant shall accept a long sale order from a customer, unless he has made a determination that the customer owns the security and will deliver in good deliverable form within three (3) business days from the execution of the order. The determination must include a notation on the order ticket at the time the order is taken which reflects the conversation with the customer as to the present location of the securities, whether they are in good deliverable form, and the customer's ability to make delivery.

(e) Execution of Short Sale. No Trading Participant shall use any facility of the Exchange to effect a short sale of any security unless (1) at a price higher than the last sale or (2) at the price of the sale if and only if that price is above the next preceding different sale price on such day.

(f) Failure to Deliver. No person shall, directly or indirectly, by the use of any facility of the Exchange, effect a short sale in a security registered or listed on the Exchange, where the seller does not intend to make delivery of the securities within the period specified in the contract. Failure on the part of the seller to make delivery on such date will be taken by **CMIC** as prima facie evidence of the lack of intention on his part to make such delivery.

(g) Mandatory Close-Out. A contract involving a short sale which has not resulted in a delivery by the Trading Participant within the settlement period must be closed by the Trading Participant by purchasing for cash or guaranteed delivery securities of like kind and quantity on the next business day after settlement date, unless such purchase cannot be effected within said period for justifiable reasons.

(h) Directors, Officers or Principal Stockholders. No director, officer or principal stockholder of a corporation shall make a short sale in securities of the corporation in which he is a director, officer or principal stockholder.

(i) Order for Short Sale. Upon receiving an order to sell short, the same should be indicated on the selling order and throughout all the records pertinent to the sale. Prior to acceptance of any short sale order, the Trading Participant shall arrange to borrow the securities to make delivery by settlement date.

(j) Exempt Transaction. This Rule notwithstanding, the Exchange **and/or CMIC** may prohibit short selling indefinitely or for such period of time as it may deem necessary or advisable for the protection of investors.

Section 11. *Client Confirmation.* (a) A Trading Participant shall report to its customers all transactions entered into for the customer's account, provided that a verbal confirmation made on the same day and followed by a written confirmation shall be deemed a compliance with the confirmation requirement. An employee or salesman

of a Trading Participant shall not be authorized to accept a confirmation for or on behalf of a customer.

(b) The Trading Participant shall give its clients the option to choose whether confirmation of customer orders will be done by way of courier, facsimile transmission or electronic mail and such preference should be clearly stated in the CAIF. The confirmation shall be sent to the customer at the address indicated in the CAIF. Parties subscribing to facsimile transmission or electronic mail confirmation of customer orders are governed by the special procedure provided in the immediately succeeding paragraph.

(c) The Trading Participant shall electronically send to its clients, during office hours and on the day of the transaction, their confirmations. Clients subscribing to such arrangements are required to attest to the accuracy of the information communicated by replying via facsimile transmission or electronic mail to the Trading Participant, not later than 12:00 noon of the next business day. The Trading Participant shall then keep a printout of such reply together with the file notifications and transaction data being confirmed.

(d) The confirmation shall contain at least the following information:

(i) A statement as to whether the Trading Participant is brokering for a customer or another Trading Participant or is dealing for himself pursuant to Section 34.1 (a) to (d) of the SRC and SRC Rule 34.1, paragraph 1;

(ii) That the Trading Participant is controlled by, or controls, or is under common control with the issuer of such security if such be the fact;

(iii) Whether the transaction was solicited or unsolicited by the Trading Participant or whether the transaction was executed pursuant to the exercise of discretionary power; and

(iv) For facsimile transmission and electronic confirmations, the reminder that clients must confirm their orders, not later than 12 noon of the next business day.

Section 12. *Customer Account Statement.* (a) A Trading Participant shall send a monthly statement of account to **each customer** containing a description of any securities positions, money balances, or account activity, to each customer whose account had a security position, money balance, or account activity during the period since the last such statement was sent to the customer. In exceptional cases and only upon written request made by the customer, the Trading Participant may issue quarterly statements in lieu of monthly statements. The written request by the customer shall be kept in the firm's files for the Commission's or CMIC's audit/investigation purposes.

(b) A Trading Participant may issue **quarterly statements to customers whose accounts have not been traded for a period of a least one (1) year (inactive accounts)**. The Trading Participant can only be excused from this obligation if, after at

least three (3) attempts, the mails (with registry cards) are returned by the post office for failure to locate the customers' whereabouts. In such cases, the Trading Participant is required to notify CMIC of the nature of these accounts and keep in its files proof that these mails were indeed returned by the post office undelivered.

(c) Notwithstanding the issuance of quarterly statements of account, the Trading Participant is still required to maintain closing balances of customers' positions every month's end and these balances must always be reflected and easily identifiable in the company's books and records. Moreover, they should be available for inspection by CMIC and/or the Commission at anytime.

(d) Such statement shall disclose that free credit balances are not segregated and may be used in the operation of the Trading Participant and that such funds are payable on demand of the customer.

(e) For purposes of this Rule, the term "account activity" shall include, but not be limited to, purchases, sales, interest credits or debits, charges or credits, dividend payments, transfer activity, securities receipts or deliveries, and/or journal entries relating to securities or funds in the possession or control of the Trading Participant.

Section 13. *Monthly Securities Counts by Trading Participants.* This Rule shall apply to all Trading Participants, except Trading Participants who promptly transmit all funds and deliver all securities received in connection with their activities as Trading Participants, and who do not otherwise hold securities for itself or hold funds or securities for, or owe money or securities to, customers.

Any Trading Participant who is subject to the provisions of this Rule shall at least once a month:

(a) Physically examine and count all securities held;

(b) Account for all securities in transit, in transfer, pledged, loaned, borrowed, deposited, failed to receive, failed to deliver, subject to repurchase and reverse repurchase agreements, or otherwise subject to its control or direction but not in its physical possession by examination and comparison of the supporting detail records with the appropriate ledger control accounts;

(c) Verify all securities in transfer, in transit, pledged, loaned, borrowed, deposited, failed to receive, failed to deliver, subject to repurchase and reverse repurchase agreements, or otherwise subject to its control or direction but not in its physical possession, where such securities have been in that status for longer than thirty (30) days;

(d) Compare the results of the count and verification with its records; and

(e) Record on its books and records all unresolved differences setting forth the security involved and date of comparison in a security count difference account no later than seven (7) business days after the date of each required quarterly security examination, count and verification. Provided, however, that no examination, count, verification and comparison for the purpose of this rule shall be within two (2) months of or more than four (4) months following a prior examination, count, verification and comparison made hereunder.

The examination, count, verification and comparison may be made either as of a date certain or on a cyclical basis covering the entire list of securities. In either case the recording shall be effected within seven (7) business days subsequent to the examination, count, verification and comparison of a particular security. In the event that an examination, count, verification and comparison is made on a cyclical basis, it shall not extend over more than one calendar quarter, and no security shall be examined, counted, verified or compared for the purpose of this rule less than two (2) months or more than four (4) months after prior examination, count, verification and comparison.

The examination, count, verification and comparison shall be made or supervised by persons whose regular duties do not require them to have direct responsibility for the proper care and protection of the securities or the making or preservation of the relevant records.

The Commission and/or **CMIC** may, upon written request, exempt from the provisions of this rule, either unconditionally or on specified terms and conditions, any Trading Participant who satisfies **CMIC** that it is not necessary in the public interest and for the protection of investors to subject that particular Trading Participant to certain or all of the provisions of this rule because of the special nature of the Trading Participant's business, the safeguards it has established for the protection of customers' funds and securities, or such other reasons as may be deemed appropriate.

Section 14. *Buy-in of Short Security Differences.* A Trading Participant shall, within ten (10) days after the date of the examination, count, verification and comparison of securities pursuant to these Rules and SRC Rule 52.1, paragraph 10 or for the preparation of the annual report of financial condition in accordance with SRC Rule 52.1, paragraph 5, or for any other purpose, buy-in all short security differences which are not resolved during the ten (10) day period. This requirement is without prejudice to the independent determination by the Commission or **CMIC** of the Trading Participant's liability pursuant to the other provisions of the Code and the Rules.

Section 15. *Obligation of Trading Participant with respect to the Physical Possession and Control of Securities.* A Trading Participant, on a daily basis, shall obtain and shall thereafter maintain the physical possession or control of all fully paid securities and excess margin securities carried by a Trading Participant for the account of customers.

A Trading Participant shall not be deemed to be in violation of the provisions on

the physical possession or control of customers' securities if, solely as the result of normal business operations, temporary lags occur between the time when a security is required to be in the possession or control of the Trading Participant and the time that it is placed in the firm's physical possession or under the firm's control; provided, the Trading Participant takes timely steps in good faith to establish prompt physical possession or control.

The burden of proof shall be on the Trading Participant to establish that the failure to obtain physical possession or control of securities carried for the account of customers is merely temporary and solely the result of normal business operations including same day receipt and redelivery (turnaround), and to establish that the Trading Participant has taken timely steps in good faith to place them in the Trading Participant's physical possession or control.

A Trading Participant shall not be deemed to be in violation of the provisions regarding physical possession or control of fully-paid or excess margin securities borrowed from any person, provided, that the Trading Participant and the lender, at or before the time of the loan, enter into a written agreement that, at a minimum;

(a) Sets forth in a separate schedule or schedules, the basis of compensation for any loan and generally, the rights and liabilities of the parties as to the borrowed securities;

(b) Provides that the lender will be given a schedule of the securities actually borrowed at the time of the borrowing of the securities;

(c) Specifies that the Trading Participant shall:

(i) Provide to the lender, upon the execution of the agreement or by the close of the business day of the loan if the loan occurs subsequent to the execution of the agreement, collateral consisting exclusively of cash or Republic of the Philippines treasury bills and treasury notes or an irrevocable letter of credit issued by a bank which fully secures the loan of securities, and

(ii) Must mark the loan to the market daily and, in the event the market value of all the outstanding securities loaned at the close of trading at the end of the business day exceeds 100 percent of the collateral then held by the lender, the borrowing Trading Participant must provide additional collateral of the type described in subparagraph (i) above to the lender by the close of the next business day as necessary to equal, together with the collateral then held by the lender, not less than one hundred percent (100%) of the market value of the securities loaned;

Section 16. *Control of Securities.* Securities under the control of a Trading Participant shall be deemed to be securities which:

(a) Are represented by one or more certificates in the custody or

control of a central depository and/or a clearing agency registered with the Commission in accordance with Section 42 of the SRC, the delivery of which certificates to the Trading Participant does not require the payment of money or value, and if the books or records of the Trading Participant identify the customers entitled to receive specified number or units of the securities so held for such customers collectively, or

(b) Are carried for the account of any customer by a Trading Participant and are carried in a special omnibus account or Done Through Account in the name of such Trading Participant with another Trading Participant, such securities being deemed to be under the control of the Trading Participant to the extent that it has instructed such carrying Trading Participant to maintain physical possession or control them free of any charge, lien or claim of any kind in favor of such carrying Trading Participant or any person claiming through such carrying Trading Participant; or

(c) Are the subject of bona fide terms of transfer; provided that securities shall be deemed not to be the subject of bona fide items of transfer if, within forty (40) days after they have been transmitted for transfer by the Trading Participant to the issuer or its transfer agent, new certificates conforming to the instructions of the Trading Participant have not been received by him, he has not received a written statement by the issuer or its transfer agent acknowledging the transfer instructions and the possession of the securities or he has not obtained a revalidation of a window ticket from a transfer agent with respect to the certificate delivered for transfer; or

(d) Are in the custody of a foreign depository, foreign clearing agency or foreign custodian bank which the Commission upon application from a Trading Participant, **CMIC** or upon its own motion, shall designate as a satisfactory control location for securities; or

(e) Are in the custody or control of a bank the delivery of which securities to the Trading Participant does not require the payment of money or value and the bank having acknowledged in writing that the securities in its custody or control are not subject to any right, charge, security interest, lien or claim of any kind in favor of a bank or any person claiming through the bank; or

(f) Are held in or are in transit between offices of the Trading Participant; or held by a corporate subsidiary if the Trading Participant owns and exercises a majority of the voting rights of all of the voting securities of such subsidiary, assumes or guarantees all of the subsidiary's obligations and liabilities, operates the subsidiary as a branch office of the Trading Participant, and assumes full responsibility for compliance by the subsidiary and all of its salesmen and other personnel with the provisions of the Code and rules and regulations adopted thereunder as well as for all of the other acts of the subsidiary and such persons; or

(g) Are in transit to or from Trading Participants, banks, custodians,

registered transfer agents and registered clearing agencies which are otherwise good control locations pursuant to the term of this Rule, provided, such items shall have been in transit from or to the Trading Participant for a period of not more than five (5) business days from the day they are first put in transit, and provided further, the books and records of the Trading Participant clearly account for such items. An "in transit" account may be used for this purpose; or

(h) Are held in such other locations as the Commission shall, upon application from a Trading Participant or **CMIC**, find and designate to be adequate for the protection of customer securities.

Section 17. Requirement to Reduce Securities in Possession or Control. Not later than the next business day, a Trading Participant, as of the close of the preceding business day, shall determine from the Trading Participant's books or records, the quantity of fully paid securities and excess margin securities in its possession or control and the quantity of fully paid securities and excess margin securities not in its possession or control. In making this daily determination, inactive margin accounts (accounts having no activity by reason of purchase or sale of securities, receipt or delivery of cash or securities or similar type events) may be computed once a week.

If such books or records indicate, as of the close of the business day, that the Trading Participant has not obtained physical possession or control of all fully paid and excess margin securities as required by this paragraph, and there are securities of the same issue and class in any of the following non-control locations:

(a) Securities subject to a lien securing monies borrowed by the Trading Participant or securities loaned to another Trading Participant, then the Trading Participant shall, not later than the business day following the day on which such determination is made, issue instructions for the release of such securities from the lien or return such loaned securities and obtain physical possession or control of such securities within two (2) business days following the date of issuance of the instructions in the case of securities subject to lien securing borrowed monies and within five (5) business days following the date of issuance of instructions in the case of securities loaned; or

(b) Securities included on his books or records as failed to receive more than thirty (30) days, then the Trading Participant shall, not later than the business day following the day on which such determination is made, take prompt steps to obtain physical possession or control of securities so failed to receive through a buy-in procedure or otherwise; or

(c) Securities receivable by the Trading Participant as a stock dividend receivable, stock split, or similar distribution for more than forty-five (45) days, then the Trading Participant shall, not later than the business day following the day on which such determination is made, take prompt steps to obtain physical possession or control of securities so receivable through a buy-in procedure or otherwise.

A Trading Participant which is subject to the requirements of this rule with respect to physical possession or control of fully paid and excess margin securities shall prepare and maintain a current and detailed written description of the procedures which it utilizes to comply with the possession or control requirements set forth in this rule.

A Trading Participant which is subject to this Rule shall record information relating to physical possession and control of fully paid and excess margin securities on a quarterly basis and submit such record to **CMIC**.

Section 18. *Delivery of Securities.* Nothing stated in this Rule shall be construed as affecting the absolute right of a customer of a Trading Participant to receive, in the course of normal business operations following demand made on the Trading Participant, the physical, electronic or constructive delivery of the securities for:

(a) Fully paid securities to which he is entitled, and

(b) Margin securities upon full payment by such customer of his indebtedness to the Trading Participant and, subject to the right of the Trading Participant to retain collateral for the firm's own protection beyond the requirements of this Rule and SRC Rule 48.1-1, excess margin securities not reasonably required to collateralize such customer's indebtedness to the Trading Participant.

Section 19. *Special Reserve Bank Account for the Exclusive Benefit of Customers.* Every Trading Participant shall maintain with a bank/s at all times when deposits are required or hereinafter specified a "Special Reserve Bank Account for the Exclusive Benefit of Customers" (hereinafter referred to as the "Reserve Bank Account"), and it shall be separate from any other bank account of the Trading Participant. A Trading Participant shall at all times maintain in the Reserve Bank Account, through deposits made therein, cash (by maintaining a separate bank deposit) and/or qualified securities (by opening a custody account) in amounts computed in accordance with the prescribed formula.

A Trading Participant, in addition to or in lieu of maintaining a Reserve Bank Account, may, upon proper application with and approval by **CMIC**, deposit qualified securities with duly accredited or recognized entities exercising custodianship functions, for this purpose, **CMIC** may prescribe other conditions that shall govern deposits of cash and/or qualified securities outside the banking system and with affiliated companies.

It shall be unlawful for any Trading Participant to accept or use any of the amounts under items comprising Total Credits under the formula referred to in the preceding paragraph indicated under items comprising Total Debits under the formula and, to the extent Total Credits exceed Total Debits, the net amount thereof shall be maintained in the Reserve Bank Account required herein.

Computations necessary to determine the amount required to be deposited shall be made weekly, as of the close of the last business day of the week and the deposit so

computed shall be made no later than one (1) hour after the opening of banking business on the second following business day; Provided, however, a Trading Participant which has aggregate indebtedness not exceeding 800 percent of net capital as defined in SRC Rule 49.1 and which carries aggregate customer funds as computed at the last required computation pursuant to this rule, not exceeding Php25 million may, in the alternative, make the computation monthly, as of the close of the last business day of the month, and in such event, shall deposit not less than one hundred five percent (105%) of the amount so computed no later than one (1) hour after the opening of banking business on the second following business day.

Documents supporting the deposit shall be submitted to CMIC on the 15th day of the month following the computation.

If a Trading Participant, computing on a monthly basis has, at the time of any required computation, aggregate indebtedness in excess of 800 percent of net capital, such Trading Participant shall thereafter compute weekly as aforesaid until four successive weekly computations are made, none of which are made at a time when his aggregate indebtedness exceeded 800 percent of his net capital.

Computations, in addition to the computations required herein, may be made as of the close of any other business day, and the deposits so computed shall be made no later than one (1) hour after the opening of banking business on the second following business day.

The Trading Participant shall make and maintain a record of each such computation made pursuant to this section and submit such computation quarterly to **CMIC no later than the 15th day of the month after the end of every quarter.**

Section 20. *Notification of Banks.* A Trading Participant required to maintain the Reserve Bank Account as prescribed by Section **19** this Article, shall obtain and preserve in accordance with this rule, a written notification from each bank in which the firm has its Reserve Bank Account that the bank and/or entity with custodianship arrangements (custodian) was informed that all cash and/or qualified securities deposited therein are being held by the bank and/or custodian for the exclusive benefit the Trading Participant's customers in accordance with the rules and regulations of the **CMIC**, and are being kept separate from any other accounts maintained by the Trading Participant with the bank and/or custodian. The Trading Participant shall have a written contract with the bank and/or custodian which provides that the cash and/or qualified securities shall, at no time, be used directly or indirectly as security for a loan to the Trading Participant by the bank and/or custodian and shall be subject to no right, charge, security interest, lien or claim of any kind in favor of the bank, and/or custodian, or any person claiming through the bank and/or custodian.

The Trading Participant shall at all times file with the Commission and **CMIC** a copy of the notification duly received by the bank and/or custodian.

Section 21. *Withdrawals from the Reserve Bank Account.* A Trading Participant may make withdrawals from the firm's Reserve Bank Account if and to the

extent that at the time of the withdrawal, the amount remaining in the Reserve Bank Account is not less than the amount then required this rule. A bank may presume that any request for withdrawal from a Reserve Bank Account is in conformity and compliance with this paragraph. On any business day on which a withdrawal is made, the Trading Participant shall make a record of the computation on the basis of which the firm makes such withdrawal, and the Trading Participant shall preserve such computation in accordance with SRC Rule 52.1-2.

Section 22. *Notification in the Event of Failure to Make a Required Deposit.* If a Trading Participant shall fail to make in its Reserve Bank Account a deposit, as required by this rule, the Trading Participant shall by fax, telegram or other similar means, immediately notify the Commission and **CMIC** and shall promptly thereafter confirm such notification in writing, including the reasons for such failure.

Section 23. *Lending and Voting Customers Securities.* A Trading Participant which extends credit to a customer shall not, without the written consent of the customer, lend the latter's securities to itself or to anyone else, or vote them as if they were its own.

Section 24. *Distribution of Proxies by Trading Participant.* Any Trading Participant holding securities of a registrant over which it exercises fiduciary powers in nominee name, or otherwise, who receives from a registrant an inquiry pertaining thereto shall:

- (a) Respond to such inquiry by mail or other equally prompt means no later than seven (7) business days after the date it receives such inquiry; and
- (b) Without need of any request, notice or demand from its customers who are the beneficial owners of the registrant's securities, forward the proxy, other proxy soliciting material, information statement, and/or annual report to security holders received from the registrant to said customers who are beneficial owners of the registrant's securities not later than five (5) business days after receipt of such material.

Section 25. *Consent of Customer for Use of Proxy.* No Trading Participant shall give any proxy, consent or authorization, in respect of any security carried for the account of a customer to a person other than the customer, without the express written authorization of such customer. The proxy executed by the Trading Participant shall be accompanied by a certification under oath stating that before the proxy was given to the Trading Participant, he had duly obtained the written consent of the persons in whose account the shares are held.

Section 26. *Exemptions.* The provisions of Sections 15, 16, 17, 20, 21, 22 and 23 of this Article VII shall not be applicable to a Trading Participant who carries no margin accounts, promptly transmits all customer funds and delivers all securities received in connection with its activities as a Trading Participant and does not otherwise hold funds or securities for, or owe money or securities to, customers.

Upon written application by a Trading Participant, **CMIC** may exempt such Trading Participant from the provisions of said sections, either unconditionally or on specified terms and conditions, if the Commission or **CMIC** finds that the Trading Participant has established safeguards for the protection of funds and securities of customers comparable with those provided for by said sections and that it is not necessary in the public interest or for the protection of investors to subject the particular Trading Participant to the provisions of this rule.

Section 27. *Extensions of Time.* If **CMIC** is satisfied that a Trading Participant is acting in good faith in making the application and that exceptional circumstances warrant such action, **CMIC**, on application of the Trading Participant, may extend any period specified in this Rule, relating to the requirement that such Trading Participant take action within a designated period of time to buy-in in a security, for one or more limited periods commensurate with the circumstances. **CMIC** shall make and preserve for a period of not less than three (3) years a record of each such extension granted which shall contain a summary of the justification for the granting of the extension.

Section 28. *Prohibited Transactions in Securities where Trading Participant and Issuer are Linked.* (a) No Trading Participant shall deal in or otherwise buy or sell, for its own account or for the account of customers, securities listed on the Exchange issued by any corporation where any stockholder, director, associated person or salesman, or authorized clerk of said Trading Participant and all the relatives of the foregoing within the fourth civil degree of consanguinity or affinity, is at the time holding office in said issuer corporation as a director, president, vice-president, manager, treasurer, comptroller, secretary or any office of trust and responsibility, or is a controlling person of the issuer.

(b) Every Trading Participant shall request every stockholder, director, associated person, salesman and authorized clerk of the Trading Participant (collectively referred to as "director") to complete and submit to the Trading Participant an executed copy of SEC Form 30.1 under oath (hereinafter referred to as the "questionnaire") to ensure compliance with the prohibitions set forth in Section 30.1 of the SRC.

(c) Based on information set forth in the questionnaire, every Trading Participant shall provide the Commission with a list of securities that the Trading Participant is prohibited from dealing in, purchasing or selling, and shall file an amendment thereto with the Commission, within twenty four (24) hours of any change thereto.

(d) Every director shall ensure that his questionnaire is accurate and complete at all times and shall update and submit to the Trading Participant any amendments thereto within twenty four (24) hours to reflect any change thereto.

(e) The failure of any director to comply with this rule shall be deemed a violation of the SRC.

Section 29. *Protection of Customer Accounts Where Registration of a Trading Participant is Suspended or Revoked.* Where the Commission has suspended or revoked the registration a Trading Participant under Section 29 of the Code, **CMIC** shall immediately arrange for another Trading Participant to take over any outstanding contracts relating to securities and simultaneously notify the Commission in writing of such transfer and the affected customers that said contracts have been transferred.

Section 30. *Protection of Customer Accounts in Case of Business Failure of a Trading Participant.* (a) When a Trading Participant has filed or is the subject of a petition for insolvency, or when **CMIC** determines that the Trading Participant's financial condition has so deteriorated that it cannot readily meet the demands of its customers for the delivery of securities and or payment of sales proceeds, the Commission may issue ex parte an order compelling the insolvent or failed Trading Participant and **CMIC** to take the necessary action to protect customer accounts including, but not limited to, the preservation of the Trading Participants books and records. Said order shall remain in effect until lifted by the Commission motu proprio or upon petition of the failed Trading Participant.

(b) The Commission, after proper investigation or verification, motu proprio or upon verified complaint by any party, order **CMIC** to take over the operation of the failed Trading Participant for the purpose of settling the failed Trading Participant's liabilities to its customers.

(c) Where the Commission has ordered **CMIC** to take over the operations of a failed Trading Participant, **CMIC** shall:

i. **Recommend the suspension of such failed Trading Participant's membership in the Exchange**, immediately arrange for another Trading Participant to take over the outstanding contracts relating to securities, and simultaneously notify the Commission of such suspension and takeover;

ii. Promptly notify customers of the failed Trading Participant that their accounts have been transferred to another Trading Participant and provide such customers with the opportunity to re-transfer their accounts to another Trading Participant of their choice;

iii. Settle the failed Trading Participant's liabilities to customers through the sale of its trading rights and other trade-related assets as may be prescribed by the Commission; liquidation of paid up capital; and/or overseeing the payment of claims against the surety bond.

iv. Simultaneously inform the SIPP of such takeover and inform the customers that they may also claim compensation for losses from the SIPP, subject to the validation of their claims by **CMIC** and the SIPP;

v. Where after such settlement and liquidation of the failed Trading Participant's trade-related assets, there are outstanding liabilities to customers of the failed Trading Participant, refer the same to the SIPP and inform the customers of the further steps necessary for claiming compensation for unsatisfied losses; and

vi. The SIPF, based on its rules and regulations or upon order of the Commission, shall release payments to the failed Trading Participant's customers even before **CMIC** has finalized the settlement of the failed Trading Participant's liabilities, subject to the validation as provided in subsection iv herein; Provided, however, that the SIPF shall be subrogated to the customers' rights to claim before **CMIC** to the extent that it has paid the customers' claims before final settlement of the failed Trading Participant's liabilities by **CMIC**.

(d) Business failure of a Trading Participant shall be established upon the determination by **CMIC**, or the Commission, when **CMIC** fails or does not exercise such timely determination, that the financial condition of the Trading Participant has so deteriorated that the Trading Participant cannot readily meet the demands of its customers for the delivery of securities and/or the payment of sales proceeds; Provided, however, that such determination shall not be dependent upon a judicial declaration of insolvency.

Section 31. *Best Execution.* In any transaction for or with a customer, a Trading Participant shall use reasonable diligence to ascertain the best available price for the security and buy or sell at that price so that the resultant price to the customer is as favorable as possible under the prevailing market conditions.

ARTICLE VIII. CAPITALIZATION REQUIREMENTS OF TRADING PARTICIPANTS

A. RISK BASED CAPITAL ADEQUACY REQUIREMENT

Section 1. *Definition and Coverage.* The RBCA ratio is calculated as the Trading Participant's net liquid capital divided by its total risk capital requirement. SEC Memorandum Circular No. 16 Series of 2004 requires, among others, that the RBCA for every Trading Participant be greater than or equal to 1.1.

Every Trading Participant is covered by the RBCA rules and requirements under SEC Memorandum Circular No. 16 Series of 2004.

Section 2. *RBCA Guidelines.* In monitoring compliance with the RBCA framework, CMIC, shall observe the following guidelines:

2.1. Prudential and Financial Measures.

(A) Paid Up Capital Requirement. Unless otherwise prescribed by the Commission, the paid-up capital of every Trading Participant covered by the RBCA shall be governed by the existing requirements of SRC Rule 28.1 (E) (v).

For this purpose, the term "paid up capital" shall include the following:

- (1) Capital contributions of partners or par value or stated value of Common Stock
- (2) Payment made on Subscribed Common Stock
- (3) Par or Stated Value of Preferred Stock
- (4) Payment made on Subscribed Preferred Stock
- (5) Common Stock to be Distributed (arising from a Stock Dividend Declaration)
- (6) Additional Paid in Capital for both Common and Preferred Stocks
- (7) Donated Capital

The value representing Treasury Stock is deducted in the computation of Paid up capital.

(B) Reserve Fund.

(1) Every Trading Participant shall annually appropriate a certain minimum percentage of its audited profit after tax and transfer the same to the Appropriate Retained Earnings Account in accordance with the following schedule:

| Unimpaired Paid Up Capital PhP (million) | Minimum percentage or profit after tax to be placed in the Appropriated Retained Earnings |
|---|--|
| Between 10-30 | 30% |
| Between 30- 50 | 20% |
| More than 50 | 10% |

(2) The amount appropriated shall not be available for payment of dividends.

(3) Where in any financial year the Trading Participant's paid up capital is impaired, the Trading Participant is required to transfer from the Appropriated Retained Earnings to the capital account an amount equivalent to the impairment. Such amount so transferred out shall not be available for payment of dividend.

(4) Consistent with the general usage under SRC Rule 28.1 (E) (v), the term "Unimpaired Paid Up Capital" shall refer to the firm's Total Paid Up Capital less any deficiency in the Retained Earnings account.

(5) A Trading Participant may submit to the Commission for approval its own capital build-up plan in lieu of the requirements of this provision.

(6) Notwithstanding the requirements of this section, the Commission may prescribe a different capital build up plan for all Trading Participants, specifically those incurring net losses during the period, with may include the programmed infusion of fresh capital.

(C) Reserve Requirement Account and Custody of Securities. Unless otherwise prescribed by the Commission, the responsibilities related to the setting up of a Reserve Requirement Account by every Trading Participant and the custody of securities shall be governed by the requirements of SRC Rule 49.2 (Customer Protection Reserves and Custody of Securities) and shall be observed at all times.

2.2 Financial Records and Reporting. Financial Records and Reporting shall be primarily governed by SRC Rule 52.1 (Accounts and Records, Reports, Examination of Exchanges, Members and Others) and secondarily by all pertinent provisions of the

SRC and its Implementing Rules, and all other regulations which the Commission may from time to time adopt.

With respect to compliance with the requirements on RBCA, every Trading Participant covered by the RBCA rules shall prepare its RBCA Report as of month end and file the same with the Commission and CMIC on or before the 15th of the following month. The RBCA Report shall be certified by the firm's Associated Person and President/Nominee Director and a copy submitted to the Trading Participant's Audit Committee or in lieu thereof, its Board of Directors. A pro-forma RBCA Report to be prescribed by this Commission shall form part of this Rule.

In situations where any of the financial obligations of Trading Participants as prescribed under Paragraph 2.6 (A)(A.2) is breached, the Associated Person must immediately notify the Commission, **CMIC**, and the company's Board of Directors. Proper corrective measures must be adopted by the Board to avoid suspension of operations. Daily notification by the Trading Participant is required to the Commission and **CMIC** until the breach is fixed or corrected.

In compliance with the requirements of SRC Rule 52.1 (5) (Annual Audited Financial Reports of Broker Dealers), every Trading Participant shall, in lieu of submitting a Computation of Net Capital under SRC Rule 49.1, submit the RBCA Report.

2.3 Risk Management and Internal Control.

(A) Principles of Risk Management.

(1) Every Trading Participant shall -

(a) establish, maintain and exercise effective policies and procedures on risk management; and

(b) have its own system of monitoring risk on a daily basis.

The Trading Participant should be able to describe and demonstrate the objectives and operation of the system to **CMIC** and the Commission. The policies and procedures on risk management shall be documented in a Risk Management Manual. Said manual shall be periodically updated to effect certain changes in the system. A certification from the management of the Trading Participant that the Risk Management procedures have been consistently followed should be submitted to the Commission and **CMIC no later than the first Friday of January of each year.**

(2) Every Trading Participant shall determine and record in its financial records appropriate position and credit limits for all counterparties to which it has a credit exposure.

(3) The position and credit limits established shall be appropriate to the type, nature and volume of business undertaken and the financial status of the counterparty and shall be reviewed on a regular basis, at least once a year. Every Trading Participant shall be responsible in determining the propriety of conducting more frequent reviews taking into consideration the changes in the financial condition of its counterparties.

(4) A Trading Participant's financial records shall be capable of being summarized in such a way as to permit actual exposures to be measured regularly against the established position and credit limits.

(5) A Trading Participant shall maintain its records in a manner such that they adequately disclose, or are capable of adequately disclosing, in a prompt and appropriate manner, the financial and business information which will enable its management to -

(a) identify, quantify, control and manage the Trading Participant's risk exposures;

(b) make timely and informed decisions;

(c) monitor the performance of all aspects of the Trading Participant's business on an up-to-date basis;

(d) monitor the quality of the Trading Participant's assets; and

(e) safeguard the assets of the Trading Participant and assets belonging to other persons for which the Trading Participant is responsible.

(6) Every Trading Participant's risk systems and processes should be capable of being externally and independently audited by **CMIC**, Commission or any other third party acting on behalf of **CMIC** or the Commission.

(B) Internal Control.

(1) Every Trading Participant shall establish and maintain at all times written policies and procedures on internal control and should be able to describe and demonstrate the objectives and operation of such policies and procedures to **CMIC** and the Commission.

(2) In determining the scope and nature of effective internal control, a Trading Participant shall consider all relevant factors including the size of the business, the diversity of operations, the volume, size and frequency of transactions, the degree of risk associated with each area of operation

and the amount of control by its senior management over day to day operations.

(3) The systems of internal control shall be designed in such a way as to ensure that -

(a) all transactions and commitments entered into are recorded and are within the scope of authority of the Trading Participant or the individual acting on behalf of the Broker Dealer entering into such transactions or commitments;

(b) there are procedures to safeguard assets and control liabilities, including assets belonging to other persons for which the Trading Participant is accountable;

(c) there are measures, so far as is reasonably practicable, to minimize the risk of losses to the Trading Participant from irregularities, fraud or error and to identify such matters should they occur so that prompt remedial action may be taken by the management; and

(d) there is clear delineation of responsibilities and proper segregation of tasks among the departments and the personnel of the Trading Participant.

2.4 Provisioning for Overdue Accounts.

(A) Provisions for Overdue Accounts.

(1) Definitions. For purposes of implementing the requirements on provisioning for overdue accounts, the following terms shall have their respective meanings:

(a) Amount outstanding – with respect to a particular customer account, refers to the total or aggregate receivable or collectible due from any account at any one time, inclusive of commission charges, interest charges and other relevant and reasonable charges).

(b) Contra losses – refers to all losses incurred by customers arising from contra transactions, inclusive of relevant and reasonable charges.

(c) Contra transaction – refers to a transaction where a Trading Participant allows its client to settle outstanding buy positions against outstanding sell positions of the same securities where the orders for both buy and sell orders are made within the same period

stipulated by the Commission. Unless another period is prescribed by the Commission, the period referred to is the same trading day. Also known as Off-setting.

(d) Effective date – refers to the effectivity date of the guidelines.

(e) Equity – refers to the client's/customer's required equity maintenance in the form of cash and securities needed for purposes of opening a margin account with the Trading Participant.

(f) Interest – refers to all charges and fees payable by the customer to the Trading Participant arising from a legal loan agreement or any similar arrangement.

(g) Interest-in-suspense – refers to the interest that has been suspended and credited to the interest-in-suspense account in accordance with these rules.

(h) Interest-in-suspense account – refers to the account so designated for the interest-in-suspense.

(i) Margin account – refers to the account opened and maintained by a customer for the purpose of trading securities pursuant to credit facilities extended by the Trading Participant to the customer as evidenced by a formal agreement entered into by both parties.

(j) Non-performing account – refers to customer accounts which have remained outstanding for a relatively long period as qualified under Schedule for Part 4 (found at the end of these Rules) and which requires specific and general provisioning for possible uncollectibility.

(k) Overdue purchase contract refers to a buy contract for securities which is outstanding and for which no mandatory close out could be implemented due to the following reasons:

(k.1) Securities giving rise to the outstanding position have been suspended from trading by the Exchange or the Commission;

(k.2) There is no ready market;

(k.3) Such other circumstances or causes acceptable to the Commission or upon recommendation of **CMIC**.

(B) Provisioning for Overdue Accounts.

(1) Consistent with SRC Rule 52.1 (Accounts and Records, Reports, Examination of Exchanges, Members and Others) subsection 11 (on Monthly Aging of Accounts Receivable), every Trading Participant shall provide for Specific and General Provisions for overdue accounts on **all customer accounts**.

(2) Unless otherwise prescribed by the Commission, every Trading Participant shall comply with these guidelines in the preparation of its RBCA report and audited financial statements.

(3) Every Broker Dealer shall appropriate Allowance for Doubtful Accounts (ADA) using and in accordance with the following schedule:

| <u>Classification</u> | <u>Provision</u> | <u>Base</u> |
|------------------------------|-------------------------|---|
| <u>T+0 to T+2</u> | <u>0</u> | <u>Total Receivables (TR)</u> |
| <u>T+3 to T+13</u> | <u>2%</u> | <u>TR</u> |
| <u>T+14 to T+30</u> | <u>50%</u> | <u>TR less collateral (net of haircut)</u> |
| <u>T+31 up</u> | <u>100%</u> | <u>TR less collateral (net of haircut)</u> |

The ADA is computed by getting, for each doubtful account, an amount equivalent to the provision (see table above) of the amount outstanding, net of collateral (net of haircut). Basis for the computation would be the individual accounts.

(4) Every Trading Participant must establish its own policies on the writing off of bad debts and these policies must be consistent with Philippine Accounting Standards (PAS). International Accounting Standards (IAS) may be resorted to in cases where there are no applicable PAS that addresses the issue. The Broker Dealer, within seven (7) days after effecting the write off, is required to disclose the same to the Commission and **CMIC**, provide specific details on these written off accounts of single clients where such amounts singly or in aggregate exceeds Php500,000.

2.5 Satisfactory Subordination Agreements.

(A) Subordinated Liabilities.

- (1) (a) This rule sets forth minimum and non-exclusive requirements for satisfactory subordination agreements (hereinafter “subordination agreement”). The CMIC, Commission, or Trading Participant may require or include such other provisions as may be deemed necessary to the extent that such provisions do not cause the subordination agreement to fail to meet the minimum requirements of this Rule.

The subordinated agreement shall be approved by the CMIC, if affecting an Exchange Member, or by the Commission, if affecting a non-Exchange Member. Said agreement shall take effect upon such approval.

(b) For purposes of SRC Rule 49.1 (G):

- i. A **subordination agreement** may be either a subordinated loan agreement or a secured demand note agreement.
- ii. “**Subordinated loan agreement**” shall mean a notarized agreement evidencing or governing a subordinated borrowing of cash.
- iii. The “**Collateral Value**” of any securities pledged to secure a secured demand note shall mean the market value of such securities after reducing the market value of the securities by the position risk requirements as provided in Subsection V below.
- iv. “**Payment Obligation**” shall mean the obligation of a Trading Participant in respect of any subordination agreement (i) to repay cash loaned to the Trading Participant pursuant to a subordinated loan agreement or, (ii) to return a secured demand note contributed to the Trading Participant or reduce the unpaid principal amount thereof and to return cash or securities pledged as collateral to secure the secured demand note. “**Payment**” shall mean the performance by a Trading Participant of a Payment Obligation.
- v. (v.a) **Secured demand note agreement** shall mean a notarized agreement (including the related secured demand note) entered into by a Trading Participant as

borrower and a lender, evidencing or governing the contribution of a secured demand note to a Trading Participant and the pledge of securities and/or cash with the Trading Participant as collateral to secure payment of such secured demand note.

(v.b) The secured demand note shall be a promissory note executed by the lender and shall be payable on the demand of the Trading Participant to which it is contributed; Provided, however, that the making of such demand may be conditioned upon the occurrence of any of certain events which are acceptable to the Commission and to CMIC in the case of a Trading Participant which is a member of the Exchange.

(v.c) If such note is not paid upon presentment and demand as provided for therein, the Trading Participant shall have the right to liquidate all or any part of the securities then pledged as collateral to secure payment of the same and to apply the net proceeds of such liquidation, together with any cash then included in the collateral, in payment of such note. Subject to the prior rights of the Trading Participant as pledgee, the lender, as defined herein, may retain ownership of the collateral and have the benefit of any increases and bear the risks of any decreases in the value of the collateral and may retain the right to vote securities contained within the collateral and any right to income therefrom or distributions thereon, except the Trading Participant shall have the right to receive and hold as pledgee all dividends payable in securities and all partial and complete liquidating dividends.

(v.d) Subject to the prior rights of the Trading Participant as pledgee, the lender may have the right to direct the sale of any securities included in the collateral, to direct the purchase of securities with any cash included therein, to withdraw excess collateral or to substitute cash so other securities as collateral, provided that the net proceeds of any such sale and the cash so substituted and the securities so purchased or substituted are held by the Trading Participant, as pledgee, and are included within the collateral to secure payment of the secured demand note, and provided further that no such transaction shall be permitted if, after giving effect thereto, the

sum of the amount of any cash, plus the Collateral Value of the securities, then pledged as collateral to secure the secured demand note would be less than the unpaid principal amount of the secured demand note.

(v.e) Upon payment by the lender, as distinguished from a reduction by the lender which is provided for in “Annex 49.1-2A” paragraph 6(C) or reduction by the Trading Participant as provided for in “Annex 49.1-2A” paragraph (b)(7) of the Implementing Rules and Regulations of the SRC, of all or any part of the unpaid principal amount of the secured demand note, a Trading Participant shall issue to the lender a subordinated loan agreement in the amount of such payment (or in the case of a Trading Participant that is a partnership credit a capital account of the lender) or preferred or common stock(s) of the Trading Participant in the amount of such payment, or any combination of the foregoing, as provided for in the secured demand note agreement.

- vi. **“Lender”** shall mean the person who lends cash to a Trading Participant pursuant to a subordinated loan agreement and the person who contributes a secured demand note to a Trading Participant pursuant to a secured demand note agreement.

(2) Recourse to the Subordination Agreement is viewed as a temporary relief to address RBCA requirements of Trading Participants and is not intended to replace the permanent infusion of capital by stockholders. Thus, subordinated loans shall be for a maximum period of four (4) years or for such longer period as the Commission deems appropriate, provided however, that a capital buildup plan shall be a requirement for the approval of the subordinated loan. Advances or Agreements that have been outstanding for more than four (4) years would require conversion to capital unless, during the life of the subordinated loan, an equivalent infusion of capital by way of investment is made or earnings have accumulated to an equivalent amount by reason of profitable operations, in which case compulsory conversion of the debt to equity can be dispensed with upon prior application with and approval by the Commission.

(3) In order to ensure financial viability of the Trading Participant, the CMIC, for Exchange Trading Participants, or the Commission, for non-Exchange Trading Participants, may impose additional requirements to regulate the resort to financing by way of subordination agreements and may exercise discretion in the approval of such agreements.

(4) The Minimum requirements for Subordination Agreements and Miscellaneous Provisions and the sample format of the Subordinated Loan Agreement are set forth in Annex 49.1-2A and Annex 49.1-2B respectively, of the Implementing Rules and Regulations of the SRC.

2.6 Risk Based Capital Adequacy Requirements.

(A) Risk Based Capital Adequacy Ratio Requirements (RBCA).

A.1 Definition and Interpretation

a. Definition

a.1. **Adequately secured indebtedness** shall be deemed to exist when the excess of the market value of the collateral over the amount of the indebtedness is sufficient to make the loan acceptable as a fully secured loan to banks regularly making secured loans to Trading Participants.

a.2. **Aggregate Indebtedness** shall mean the total money liabilities of a Trading Participant arising in connection with any transaction whatsoever, and includes, among other things, money borrowed, money payable against securities loaned and securities failed to receive, the market value of securities borrowed to the extent to which no equivalent value is paid or credited (other than the market value of margin securities borrowed from customers and margin securities borrowed from non-customers), customers' and non-customers' free credit balances, and credit balances in customers' and non-customers' accounts having short positions in securities, but excluding:

i. Indebtedness adequately collateralized by securities which are carried long by the Trading Participant and which have not been sold or by securities which collateralize a secured demand note in conformity with SRC Rule 49.1 (G) above;

ii. Amounts payable against securities loaned, which securities are carried long by the Trading Participant and which have not been sold or which securities collateralize a secured demand note in conformity with SRC Rule 49.1 (G);

iii. Amounts payable against securities failed to receive which securities are carried long by the Trading Participant and which have not been sold or which securities collateralize a secured demand note in conformity with SRC Rule 49.1 (G);

or amounts payable against securities failed to receive for which the Trading Participant also has a receivable related to securities of the same issue and quantity thereof which are either fails to deliver or securities borrowed by the Trading Participant;

iv. Fixed liabilities adequately secured by assets acquired for use in the ordinary course of the trade or business of a Trading Participant but not other fixed liabilities secured by assets of the Trading Participant shall be so excluded unless the sole recourse of the creditor for nonpayment of such liability is to such asset;

v. Indebtedness subordinated to the claims of creditors pursuant to a satisfactory subordination agreement in conformity with SRC Rule 49.1 (G) above;

vi. Liabilities which are effectively subordinated to the claims of creditors, but which are not subject to a satisfactory subordination agreement in conformity with SRC Rule 49.1 (G) above; by non-customers of the Trading Participant prior to such subordination, except such subordinations by customers as have been approved by **CMIC** in the case of a member of that Exchange and the Commission in the case of a firm that is not a member of an Exchange;

vii. Credit balances in accounts of general partners;

viii. Deferred tax liabilities; and

ix. Eighty percent (80%) of amounts payable against securities loaned for which the Trading Participant has receivables related to securities of the same class and issue and quantity that are securities borrowed by the Trading Participant.

a.3. **Asset or Market Liquidity Risk** means that risk that an entity will be unable to unwind a position in a financial instrument at or near its market value because of the lack of depth or disruption in the market for that instrument.

a.4. **Core Equity** – shall refer to the sum of:

i. Paid-up common stock;

ii. Paid-up perpetual and non-cumulative preferred stock;

- iii. Common stock dividends distributable;
- iv. Perpetual and non-cumulative preferred stock dividends distributable;
- v. Additional paid in Capital (also known as Surplus);
- vi. Surplus reserves excluding revaluation reserves or appraisal capital;
- vii. Opening retained earnings adjusted for all current year movements

Provided, further, that the following items shall be deducted from the Total of Core Equity:

- (a) Common stock treasury shares
- (b) Perpetual and non-cumulative preferred stock treasury shares;
- (c) Unbooked valuation reserves and other capital adjustments (such as unrealized gain in value of non-current investments)

a.5. **Counterparty** means any person or entity with or for whom a Trading Participant carries on, or intends to carry on, any dealings in securities or another asset which could be either another executing Trading Participant or a client.

a.6. **Counterparty Risk** means the risk of a counterparty defaulting on its financial obligation to a Trading Participant.

a.7. **Counterparty Risk Requirement** – means the amount necessary to accommodate a given level of its Counterparty Risk, as calculated in accordance with Subsection (A.6) Counterparty Risk Requirement.

a.8. **Customer** – shall mean any person from whom, or on whose behalf, a Trading Participant received, acquired or holds funds or securities for the account of such person, but shall not include a general, special or limited partner or director or officer of the Trading Participant, or any person to the extent that such person has a claim for property or funds which by contract, agreement or understanding, or by operation of law, is part of the capital of the Trading Participant or is subordinated to the claims of creditors of the Trading Participant. However, the term “customer” of a Trading Participant shall include another Trading Participant

(the initiating Broker as defined in SRC Rule 34.1) wherein the latter maintains separately a Dealer account and a special omnibus account in behalf of his customer with the former.

a.9. **Debt or Liability** – means borrowed funds represented by a security, instrument or public document that must be repaid by the Trading Participant, issuer, or debtor.

a.10. **Debt securities** – means securities other than equity securities which may be any of the following or of a similar nature:

- i. A debt security without call or put provisions;
- ii. A discounted security without call or put provisions;
- iii. A non-convertible preferred share;
- iv. A redeemable preferred share with a fixed and certain date for redemption;
- v. An interest in a managed collective investment scheme investing only in debt or fixed income securities, mortgages, or cash;
- vi. Any other instrument defined as such by the Commission.

a.11. **Equity per Books (also called Net Worth)** – refers to the Total Stockholders' Equity section of the Balance Sheet computed as the difference between the book values of Total Assets and Total Liabilities.

a.12. **Equity Eligible for Net Liquid Capital** – shall refer to the Equity as per Books adjusted for all other liabilities which in substance can be treated as sources of capital, less ineligible equity items, the computation of which is described in Paragraph A.3 below.

a.13. **Equity Securities** – means securities other than debt securities which may be any of the following or of a similar nature:

- i. A share other than those referred to in paragraphs (iii) and (iv) of the definition of Debt securities;
- ii. A depository receipt;
- iii. An installment receipt;

- iv. An interest in a managed collective investment scheme other than an interest referred to in paragraph (e) of the definition of Debt securities;
- v. An instrument defined as such by the Commission;

a.14. **Exchange Traded** – means traded or listed on a Registered Exchange.

a.15. **Funding Liquidity Risk** – means the risk that an entity cannot obtain the necessary funds to meet its obligations as they fall due at normal times and during a crisis.

a.16. **General Guarantees** – shall refer to general guarantees of indebtedness and acceptances (including endorsements with the character of acceptances) made by the Trading Participant for loans or indebtedness incurred or assumed by a person/individual or entity other than the Trading Participant himself.

a.17. **Indebtedness Subordinated to the claims of Creditors** – refers to subordinated liabilities as provided under Paragraph 2.5 (Satisfactory Subordination Agreements) above.

a.18. **Large Exposure Limit** – Means the maximum permissible large exposure and calculated as a percentage of Core Equity in accordance with Paragraph A.7.

a.19. **Large Exposure Risk** – means risks to which a Trading Participant is exposed whether by way of:

- i. a proportionally large amount of exposure to a particular counterparty;
- ii. a proportionally large exposure to a single issuer of debt;
- iii. a proportionally large exposure to a single equity security or single issuer group.

a.20. **Large Exposure Risk Requirement** – means the amount necessary to accommodate a given level of the Trading Participant's Large Exposure Risk, which is in excess of the Large Exposure Limit.

a.21. **Liquid Assets**– means securities or other assets which have a ready market which are realizable or capable of being converted into cash within 30 days.

a.22. **Liquid Securities** – means securities which have a ready

market as defined herein below.

a.23. **Marked to Market** – is a securities valuation method where securities are valued at their closing prices on a market day.

a.24 **Negative Exposure** – shall mean the loss due to market or price risk in the event of a default by a Trading Participant as a member of the Clearing Agency in its settlement obligations. It shall be based on the existing obligations of the Trading Participant over the last three (3) settlement periods.

a.25. **Net Liquid Capital (also called NLC)** – shall mean the Equity Eligible for Net Liquid Capital of a Trading Participant, adjusted for non-allowable current and non-current assets as described in Subsection A.3 below.

a.26. **Operational Risk** – is the exposure associated with commencing and remaining in business arising separately from exposures covered by other risk requirements. It is the risk of loss resulting from inadequate or failed internal processes, people and systems which include, among others, risks of fraud, operational or settlement failure and shortage of liquid resources, or from external events.

a.27. **Operational Risk Requirement** – means the amount calculated in accordance with Paragraph A.4 which is required to cover a level of Operational Risk.

a.28. **Position Risk (also called Market Risk)** – is the risk to which a Trading Participant is exposed to and arising from securities held by it as a principal or in its proprietary or dealer account.

a.29. **Position Risk Requirement (also called Market Risk Requirement)** – means the amount necessary to accommodate a given level of Position Risk (also called Market Risk), as calculated in accordance with Paragraph A.5.

a.30. **Ready market** – means a recognized established securities market in which exists independent bona fide offers to buy and sell so that a price reasonably related to the last sales price or current bona fide competitive bid and offer quotations can be determined for a particular security almost instantaneously and where payment will be received in settlement of a sale at such price within a relatively short time. Notwithstanding the above definition, the Commission may declare a certain security as not having a ready market on the basis of historical trading volume.

A **Ready market** shall also be deemed to exist where securities have been accepted as collateral for a loan by a bank and where the Trading Participant demonstrates to **CMIC** in the case of a member of that Exchange or the Commission in the case of a firm that is not a member of an Exchange that such securities adequately secure such loans.

a.31. **Risk Based Capital Adequacy Ratio (also called RBCA Ratio)** – means the ratio linking the net liquid capital to the Trading Participant's total risk exposure (Total Risk Requirement), calculated as the Trading Participant's Net Liquid Capital (NLC) divided by its Total Risk Capital Requirement (TRCR).

a.32. **Total Risk Capital Requirement (TRCR)** is the sum of:

- i. Operational Risk requirement
- ii. Credit Risk Requirement which include requirements for Counterparty Risk, Settlement Risk, Large Exposure Risk, and Margin Lending/Financing Risk
- iii. Position or Market Risk Requirement

a.33. **Trading Participant** – shall refer to any Broker Dealer, Broker or Dealer registered by the Commission under the Securities Regulation Code and its implementing rules and regulations.

a.34 **Securities Borrowing and Lending** – refers to any transaction by the Trading Participant under an equity or debt security lending and borrowing agreement, a repurchase or reverse repurchase agreement or an agreement for the sale and buyback of the security or other similar agreement as prescribed by the CMIC and duly approved by the Commission and, subject to appropriate tax laws, by the Bureau of Internal Revenue.

b. Interpretation. The RBCA provisions should be applied and understood in relation to the SRC and its implementing rules and regulations. In case of doubt, the RBCA should be interpreted in a manner that is consistent with the SRC and its implementing rules and regulations and international best practices in financial services regulation. When in need of policy direction or legal interpretation, the Trading Participant must seek guidance from the Commission's Market Regulation Department. In choosing the appropriate treatment of financial transactions which impact on the RBCA

computation, the choice should be that which would provide a more conservative computation of RBCA ratio.

A.2 Obligations of Trading Participants.

a. General Obligations:

a.1. Every Trading Participant shall ensure that:

- i. Its Risk Based Capital Adequacy Ratio is greater than or equal to 1.1.
- ii. Its Core Equity is at all times greater than its Operational Risk Requirement. In case of breach, the Trading Participant shall be allowed to continue its operations provided that it shall submit a capital build plan which should be realized within ninety (90) calendar days from time of breach.
- iii. The Special Reserve Bank Account created for the Exclusive Benefit of Customers shall be maintained by the Trading Participant as prescribed under SRC Rule 49.2 (Customer Protection Reserves and Custody of Assets) and mentioned in Part I (Rule 49.C) of this Rule. Qualified Securities maintained in the Reserve Custody Account pursuant to the said SRC Rule shall be subject to the appropriate position risk requirement.
- iv. Every Trading Participant shall, at all times, have and maintain an NLC of at least Five Million Pesos (Php5,000,000.00) or five percent (5%) of his aggregate indebtedness whichever is higher. However, a Trading Participant who deals only with proprietary shares and who does not keep the shares under its custody shall have and maintain a net capital of Php2.5 Million Pesos or two and one-half percent (2.5%) of his aggregate indebtedness, whichever is higher. In cases where, in order to meet the RBCA ratio of at least 1.1, an NLC higher than Five Million Pesos (Php5,000,000) or five percent (5%) of aggregate indebtedness is required, the higher NLC shall be maintained.

The Commission may prescribe a lower or higher minimum NLC depending on the effectiveness of the risk management systems adopted by Trading Participants, their ability to instantaneously respond to various risks as a result of daily monitoring and reporting on capital adequacy

levels, and other developments in the market that would impact on the risk exposure levels of the firms.

v. In computing position (or market) and counterparty risk exposures, all assets shall be marked to market daily.

a.2. Notwithstanding the monthly reporting to be made to the Commission and CMIC on its RBCA as of month end, every Trading Participant shall compute its Net RBCA Margin and RBCA Ratio on a daily basis and these working papers will form part of the Books and Records of the firm. The Commission or CMIC, in the case of a member of an Exchange, may require Trading Participants from time to time to submit reports which reflect their RBCA Ratio and Margin. In such cases, the Trading Participant shall immediately submit said reports to the CMIC or the Commission.

a.3. Every Trading Participant shall immediately cease doing business as a Trading Participant, and shall notify the CMIC and the Commission if (i) the minimum Risk Based Capital Adequacy Ratio of 1.1 or (2) the minimum NLC is breached.

Should the Trading Participant fail to cease doing business upon breaching the minimum RBCA ratio or NLC requirements, the CMIC Board shall order the temporary suspension of the Trading Participant until such requirements are complied with.

b. No Trading Participant shall permit its aggregate indebtedness to all other persons to exceed 2,000 percent of its NLC. **In case of breach, the Trading Participant should cease doing business as a Trading Participant, and shall notify the CMIC and the Commission.**

Should the Trading Participant fail to cease doing business upon breaching the 2,000 percent ratio of AI to NLC, the CMIC Board shall order the temporary suspension of the Trading Participant until such requirements are complied with.

c. Notwithstanding the requirement in paragraphs A & B above, every Trading Participant shall notify the Commission in writing within twenty four (24) hours, the occurrence of any of the following events:

c.1 The Trading Participant's computation shows that its Aggregate Indebtedness is in excess of 1,700 percent of its NLC; and /or

c.2 The Trading Participant's computation shows that its Risk Based Capital Adequacy Ratio is less than 1.2; or

The Trading Participant shall, upon immediate notification, take all necessary action to increase its NLC or reduce its total risk exposure. CMIC, upon prior consultation with the Commission, or the Commission may, after receipt of such notice, direct the Trading Participant in its conduct of its operations and/or impose conditions, if necessary.

The Trading Participant is given ten (10) calendar days within which to effect its proposal. Pending actual implementation, the Trading Participant is required to notify the Commission on a daily basis of its NLC position.

d. Limitations on Withdrawal of Core Equity

d.1 No equity capital of a Trading Participant may be withdrawn by action of a stockholder or a partner or by redemption or repurchase of shares of stock or through the payment of dividends or any similar distribution, nor may any unsecured advance or loan be made to a stockholder, partner, sole proprietor, employee or affiliate, if after giving effect thereto and to any other such withdrawals, advances or loans and any payments under satisfactory subordination agreements in conformity with SRC Rule 49.1 (G) above which are scheduled to occur within one hundred and eighty (180) days following such withdrawal, advance or loan if:

i. The Trading Participant's NLC would be less than one hundred twenty percent (120%) of the minimum amount required by paragraph (A) of this rule; or,

ii. The aggregate indebtedness of the Trading Participant exceeds one thousand five hundred percent (1500%) of its net capital.

d.2. This, however, shall not preclude a Trading Participant from making required tax payments or preclude the payment to partners of reasonable compensation, and such payments shall not be included in the calculation of withdrawals, advances, or loans for purposes of paragraph D above.

d.3. For the purpose of this section, any transaction between a Trading Participant and a stockholder, partner, sole proprietor, employee or affiliate that results in a diminution of the Trading Participant's net capital shall be deemed to be an advance or loan of net capital.

A.3 Computation of Net Liquid Capital (NLC).

a. General Principles. In computing NLC, all non-allowable assets/equities, and collateralized liabilities will be deducted and allowable liabilities and equities are added to Equity per Books.

b. Computation of Equity Eligible for Net Liquid Capital. Equity Eligible for Net Liquid Capital shall be the sum of the following:

b.1 Equity as per Books;

b.2 Liabilities of the Trading Participant which are subordinated to the claims of creditors pursuant to a satisfactory subordination agreement in conformity with SRC Rule 49.1 paragraph 2 and in accordance with the following schedule:

| Period remaining from RBCA Computation date to maturity date | Allowable Inclusion |
|---|------------------------|
| 3 years 1 day to 4 years | 100% |
| 2 years 1 day to 3 years | 75% |
| 1 year 1 day to 2 years | 50% |
| 1 year or less | 0% |

b.3 In the case of a Trading Participant who is a sole proprietor, the excess of liabilities which have not been incurred in the course of business as a Trading Participant over assets not used in the business.

b.4 Deposit for Futures Stock Subscription for which an application for increase in capital stock or request for exemption for registration has been filed with the Commission and the subscription, which is in the form of Allowable Assets, shall not be withdrawn prior to SEC approval of the application/request. For net capital purposes, **Deposit for Futures Stock Subscription for which no application for increase in capital stock or request for exemption for registration has been filed with the Commission** shall be considered part of aggregate indebtedness unless there is evidence that such amount is a deposit but an irrevocable subscription or a subordinated loan agreement has been entered into with the subscriber.

Provided, further, that the following items shall be excluded from Eligible Equity for Net Liquid Capital:

(1) Deferred Income Tax;

- (2) Revaluation Reserves;
- (3) Minority Interest and any outside investment in affiliates and associates

c. Computation of Net Liquid Capital (NLC). In computing NLC, the Equity Eligible for Net Liquid Capital of a Trading Participant is adjusted by the following, provided, however, that in determining net worth, all long and all short securities position shall be marked to their market value:

c.1. Deducting fixed assets and assets which cannot be readily converted into cash [less any indebtedness excluded in accordance with paragraph (iv) of the Definition of the term Aggregate Indebtedness] including, among other things:

i. Real estate; furniture and fixtures; Exchange memberships/trading rights; prepaid rent, insurance and other expenses; goodwill, organization expenses;

ii. All unsecured advances and loans; deficits in customers' and non-customers' unsecured and partly secured notes; deficits in special omnibus accounts or similar accounts carried on behalf of another Trading Participant, after application of calls for margin, marks to the market or other required deposits that are outstanding three (3) business days or less; deficits in customers' and non-customers' unsecured and partly secured accounts after application of calls for margin, marks to the market or other required deposits that are outstanding three (3) business days or less, except deficits in cash accounts for which no more than one extension respecting a specified securities transaction has been requested and granted; the market value of stock loaned in excess of the value of any collateral received therefore; and any collateral deficiencies in secured demand notes in conformity with SRC Rule 49.1 (G) .

For the purpose of the above, a loan or any other form of receivables shall be considered "unsecured" unless the following conditions exist:

- (1) the receivable is secured by collateral which is otherwise unencumbered *provided, however*, that such receivable will be considered secured only to the extent of the market value of such collateral after application of such percentage deductions as may be prescribed by the Commission;
- (2) the collateral is in the possession or control of the Trading Member; and

- (3) the Trading Participant has a legally enforceable written security agreement executed by the debtor in its favor under which the Trading Member shall have the power to readily sell or otherwise convert the collateral into cash.
 - (4) the collateral is liquid in nature and in any of the following forms:
 - (a) Cash deposit in Philippine peso;
 - (b) Cash deposit in foreign currency acceptable to the Commission;
 - (c) Securities listed in the Exchange or other recognized stock exchanges unless specified by the Commission as not having a ready market;
 - (d) Government bonds or other debt instruments which have a ready market; and
 - (e) Any other collaterals which may be specified by the Commission as having a ready market;
- iii. Interest receivable, floor brokerage receivable, commissions receivable from other Trading Participants, and management fees receivable from registered investment companies, all of which receivables are outstanding longer than thirty (30) days from the date they arose; dividends receivable outstanding longer than thirty (30) days from the payable date;
- iv. Insurance claims which, after fifteen (15) business days from the date the loss giving rise to the claim is discovered, are not covered by an opinion of an outside counsel that the claim is valid and is covered by insurance policies presently in effect; insurance claims which after thirty (30) business days from the date the loss giving rise to the claim is discovered and which are accompanied by an opinion of outside counsel described above, have not been acknowledged in writing by the insurance carrier as due and payable; and insurance claims acknowledged in writing by the carrier as due and payable outstanding longer than twenty (20) business days from the date they are so acknowledged by the carrier;
- v. All other unsecured receivables; all assets doubtful of collection less any reserves established therefore; the amount by which the market value of securities failed to receive

outstanding longer than thirty (30) days exceeds the contract value of such fails to receive;

vi. Any receivable from an affiliate of the Trading Participant (not otherwise deducted from net worth) and the market value of any collateral given to an affiliate (not otherwise deducted from net worth) to secure a liability over the amount of the liability of the Trading Participant unless the books and records of the affiliate are made available for examination when requested by the Commission or CMIC, where the Trading Participant is a member for the Trading Participant, in order to demonstrate the validity of the receivable or payable, or when the affiliate is a financial intermediary or entity duly registered and regulated by another government agency and that the receivable arises from an arm's length transaction. The provisions of this subsection shall not apply where the affiliate is a Trading Participant;

vii. A future income tax benefit (Deferred Income Tax)

viii. Any deposit with or loan to a person other than:

(1) A deposit or loan with a deposit taking institution duly authorized and registered with the Bangko Sentral ng Pilipinas (BSP);

(2) A deposit or loan to the extent the balance is secured by collateral which is Liquid, evidenced in writing and valued at the Marked to Market value or another valued approved by the Commission;

(3) A deposit of funds as a margin to the extent that those funds relate to an open position;

ix. A deposit with a third party clearing organization, unless approved by the Commission;

x. A Related Party/Associated Person Balance to the extent that the balance is not secured by collateral which is Liquid, evidenced in writing and valued at the Marked to Market value or to another value approved by the Commission;

xi. A debt which was reported or created more than 30 days previously other than a debt:

(1) from another Trading Participant that is not a Related Party or Associated Person; or

- (2) which is secured by collateral which is Liquid, evidenced in writing and valued at the Marked to Market value or to another valued approved by the Commission;
- xii. Any prepayment which is not Liquid;
- xiii. A Liquid Asset which has been restricted for the purpose of obtaining or creating a non-allowable or illiquid asset or set aside for use outside the ordinary course of the Trading Participant's securities business;
- xiv. All other assets which are not Liquid and those prescribed by the Commission as such;

c.2. Deducting general guarantees and indemnities for loans and indebtedness other than those incurred by the Trading Participant, unless otherwise permitted by CMIC and Commission; Provided, however, that where the Trading Participant guarantee is given to a company within the Trading Participant's group of companies, that company's assets and liabilities (to the extent that they are covered by the Trading Participant's guarantee) shall be taken into account as being part of the Trading Participant's assets and liabilities for purposes of computing NLC, and in such case the guarantee shall not be deducted from the computation unless CMIC or Commission provides otherwise.

c.3. Deducting long and short securities differences as follows:

- i. Deducting the market value of all short securities differences (which shall include securities positions reflected on the securities record which are not susceptible to either count or confirmation) unresolved after discovery;
- ii. Deducting the market value of any long securities differences, where such securities have been sold by the Trading Participant before they are adequately resolved, less any reserves established therefore;
- iii. For an Exchange member, CMIC, and in the case of a Broker Dealer that is not a member of an Exchange, the Commission may extend the periods in paragraph A.3.c.2.ii above of this section for up to ten (10) business days if it finds that exceptional circumstances warrant an extension.

c.4. Deducting Negative Exposure.

A.4. Operational Risk.

a. General Principles. Every Trading Participant shall always ensure that its Operational Risk Requirement is always less than its Core Equity.

b. Computation of Operational Risk Requirement

b.1. The Trading Participant's Operational Risk Requirement shall be computed as:

| | | |
|------------|----------|---|
| 20% | x | Average of last 3 years' Gross Revenue |
|------------|----------|---|

b.2. The 3-year average gross revenue value shall be calculated on the basis of the audited financial statements of the last three (3) years immediately preceding the date of reporting which have been filed and submitted with the Commission.

For this purpose, the term "**Gross Revenue**" shall refer to all sources of revenue of the Trading Participant, net of any relevant final tax, if any, which include among, others:

- a. Commission Income
- b. Interest Revenue
- c. **Net unrealized gain from** marketable securities
- d. Rental Revenue
- d. Dividend Revenue
- e. Gain on sales of marketable securities and other assets
- f. Other gains/revenues

For purposes of computing "**Gross Revenue**," losses are not netted against revenue accounts.

b.3. The Commission or CMIC, upon prior consultation with the Commission, may include or exclude certain revenue items for purposes of determining the basis for the computation of the Operational Risk Requirement. Inclusion by the Commission of other sources of revenue in the computation of "Gross Revenue" shall not be construed as approval by the Commission for the Trading Participant to engage in activities inconsistent with or prohibited by its secondary registration or primary franchise.

b.4. The Commission or CMIC, upon prior consultation with the Commission, may require a Trading Participant to increase its Operational Risk Requirement or set a minimum amount of operational risk requirement if the Commission or CMIC is not satisfied that the internal control systems, corporate governance, personnel staffing, Written Supervisory Procedures and other similar processes are adequate.

A.5 Position Risk.

a. General Principles. Every Trading Participant shall compute its Position Risk Requirements for all equity, debt, and foreign exchange positions held by it as principal in accordance with the following conditions:

a.1. In addition to the requirements of SRC Rule 52.1, every Trading Participant shall record separately securities held for trading purposes and those held for investment purposes. The securities in the Trading Participant's books that are held for trading purposes shall form part of the computation of NLC and subject to position risk requirements while securities held for investment purposes shall be excluded in the computation of NLC and not subject to position risk requirements.

a.2. Equity securities shall be classified according to (1) Equities in PSEi; (2) Other Equities outside the PSEi; and (3) Equities not Listed in the Exchange but proven to be marketable, with separate position risk factors being applied to each category as provided in Schedule A of SEC Memorandum Circular No. 16 series of 2004;

a.3. Debt securities shall be classified according to (1) Republic of the Philippine Bonds; and (2) Other Corporate Debts with separate position risk factors being applied to each category as provided in Schedule A of SEC Memorandum Circular No. 16 series of 2004;

a.4. Foreign Currency positions shall likewise be subject to a position risk requirement as provided in Schedule A of SEC Memorandum Circular No. 16 series of 2004;

a.5. All debt and equity securities shall be marked to market using the closing prices of the immediately preceding trading day;

a.6. Where a Trading Participant has a position in an instrument or security for which no risk treatment is provided under this section, the Trading Participant must immediately seek clarification or guidance from the Commission's Market Regulation Department

on the appropriate treatment. Pending Commission action, the Position Risk Requirement shall be one hundred percent (100%) of the marked to market value of the said instrument or security.

b. Computation of Position Risk Requirement

b.1. **Position Risk Requirement** shall be computed as follows:

| | | | | |
|---------------------------|---|---|---|----------------------|
| Position Risk Requirement | = | Marked to Market value of the Instrument/Security | x | Position Risk Factor |
|---------------------------|---|---|---|----------------------|

b.2. Position Risk Factors. Position Risk Factors are presented in Schedule A of SEC Memorandum Circular No. 16 series of 2004.

b.3. Principle on Netting of long and short positions

i. Netting on long equity position against a short position is allowed provided the positions are of the same type of security.

A.6. Counterparty Risk Requirement.

a. General Principles.

a.1. The Trading Participant shall calculate its Counterparty Risk Requirement for any of the following counterparty exposures:

- i. Unsettled customer trades (arising from customer-to-broker agency relationship)
- ii. Unsettled principal trades (arising from broker-to-broker or broker-to-Exchange/Clearing Agency relationship);
- iii. Loans and other dues;
- iv. Free deliveries;
- v. Securities lending and borrowing;
- vi. Margin Lending;
- vii. Sub-underwriting arrangements or best efforts underwriting arrangements;
- viii. Other exposures as determined by **CMIC** or Commission.

a.2. In the computation of the Counterparty Risk Requirement, the following rules would apply:

i. Counterparty Risk Requirement shall be computed only for negative exposures to a counterparty and not for positive exposures.

ii. Counterparty Risk Requirement shall be calculated daily.

iii. Counterparty Exposures are marked to market.

iv. Reduction of Counterparty Risk Requirement is allowed to the extent of any of the following:

(a) the amount of collateral that was put up to support the exposure;

(b) the amount of provisions made on the exposure

v. Offsetting of positive and negative counterparty exposures prior to calculation of Counterparty Risk Requirement is allowed provided that:

(a) they are of the same counterparty;

(b) they are similar in nature in that they fall within the same class or category as enumerated in a.1 above; and

(c) The Trading Participant has a valid and binding netting agreement with the counterparty.

vi. Counterparty Risk Requirement shall be computed for all counterparty exposures regardless of the relationship between the Trading Participant and its counterparty.

a.3 Any other instrument which cannot be properly classified for counterweighting or is not in its standard form, shall have a Counterparty Risk Requirement for its full marked to market value, net of any collateral or discounts, until such time that the Trading Participant obtains guidance from the Commission's Market Regulation Department on the proper treatment of such instrument or exposure.

a.4 CMIC or the Commission may set a higher Counterparty Risk Requirement if, in its own judgment, the Trading Participant

may be exposed to material potential losses arising from any counterparty transaction unless the Trading Participant can provide documentation or proof acceptable to CMIC and Commission that its counterparty can commit to meet its obligations upon maturity. Acceptable proof may include evidence of financial standing, adequate security, or acceptable guarantees.

b. Computation of Counterparty Risk Requirement

b.1. Counterparty Risk Requirement shall be computed as follows:

| | | | | | | |
|---|---|----------------------------------|---|-----------------------------------|---|--------------------------------|
| Counterparty Risk Requirement (CRR) | = | Counterparty Exposure (CE) | x | Counterparty Weighting (CW) | x | Credit Risk Factor (CRF) |
|---|---|----------------------------------|---|-----------------------------------|---|--------------------------------|

b.2 Counterparty Weighting (CW), which is determined on the basis of the type of counterparty, is provided in Schedule B.1 of SEC Memorandum Circular No. 16 series of 2004.

b.3 Credit Risk Factor (CRF), which is determined on the basis of the type or nature of counterparty exposure risk, is provided in Schedules B.2 to B.5 of SEC Memorandum Circular No. 16 series of 2004. In the absence of a specific prescription as to the CRF to be applied to a particular counterparty exposure, the CRF to be used is 8%.

b.4. Unsettled customer trades (arising from customer-to-broker agency relationship)

i. A counterparty exposure of this kind occurs when (a) the customer poses the possible risk of failing to deliver securities on a sell contract or (b) the customer poses the possible risk of failing to pay cash on a buy contract.

ii. A negative counterparty exposure exists when the current market value exceeds the transaction value of the stock in a sell contract. A positive counterparty exposure exists when the current market value is less than the transaction value of the stock in a sell contract.

iii. A negative counterparty exposure exists when the transaction value exceeds the current market value of the stock in a buy contract. A positive counterparty exposure exists when the transaction value is less than the current market value of the stock in a buy contract.

iv. Computation of the Counterparty Risk Requirement on unsettled customer trades shall be made in accordance with Schedule B.2 of SEC Memorandum Circular No. 16 series of 2004.

b.5. Unsettled principal trades (arising from broker-to-broker or broker-to-Exchange/Clearing Agency relationships):

i. A counterparty exposure risk of this kind occurs when (a) the Trading Participant poses the possible risk of failing to receive cash from its counterparty on a sell contract or (b) the Trading Participant poses the possible risk of failing to receive the securities from its counterparty on a buy contract.

ii. A negative counterparty exposure exists when the transaction value exceeds the current market value of the stock in a sell contract. A positive counterparty exposure exists when the transaction value is less than the current market value of the stock in a sales contract.

iii. A negative counterparty exposure exists when the current value exceeds the transaction value of the stock in a buy contract. A positive counterparty exposure exists when the current value is less than the transaction value of the stock in a buy contract.

iv. Computation of the Counterparty Risk Requirement on unsettled principal trades shall be made in accordance with Schedule B.3.

b.6 Debts/Loans, contra losses and other amounts due:

i. A Trading Participant has a counterparty exposure if a debt/loan, receivable from a customer/client, contra loss, or any other amount due is not paid on its agreed due date. In the case of a contra loss, the due date shall be the date of the contra.

ii. Computation of the Counterparty Risk Requirement on debts/loans, contra losses and other amounts due shall be made in accordance with Schedule B.4 of SEC Memorandum Circular No. 16 series of 2004.

b.7. Free Deliveries

i. A free delivery happens when the trade results from a delivery of the security or any other financial instrument to a

counterparty without receiving payment or where payment is made without receiving a security or any other financial instrument.

ii. The Counterparty exposure in such cases shall be the contract value of the transaction or trade and the computation of the Counterparty Risk Requirement on free deliveries shall be made in accordance with Subsection A.6 (b) above.

iii. Notwithstanding the computation in Subsection A.6 (b.7) (ii) above, where delivery or settlement is not made within three (3) trading days from due date, the Counterparty Risk Requirement of the Trading Participant shall be the full contract value of the transaction.

iv. For this purpose, due date shall refer to:

(a) The date of the delivery by the Trading Participant on deliveries without receiving payment from the counterparty.

(b) The date of payment by the Trading Participant on payments for securities without receiving securities from the counterparty.

b.8. Securities Borrowing and Lending

i. A counterparty risk exposure exists in Securities Borrowing and Lending in the following instances:

(a) For borrowing transactions, the difference between the market value of the deposit (plus accrued interest) and the value of the securities received.

(b) For lending transactions, the difference between the market value of the securities on lend (plus unpaid fees) and the value of the collateral received.

ii. Computation of the Counterparty Risk Requirement on securities borrowing and lending shall be made in accordance with Subsection b.1 above.

b.9. Margin Financing Lending

i. For trades in Financial Instruments which are margined, the counterparty risk amount shall be:

(a) the full value of the outstanding settlement amount, premium, deposit, margin call or minimum margin maintenance that the counterparty (customer) is required to pay to the Trading Participant, regardless of whether or not the Trading Participant is required to pay that amount to an Exchange, clearing house or other entity;

(b) the full value of the outstanding settlement amount, premium, deposit, margin call or minimum margin maintenance that is due from an entity with respect to client or house trades cleared by that entity;

ii. The counterparty risk shall commence at the time that amounts are normally scheduled for payment to the relevant exchange or clearing house.

iii. A Trading Participant may reduce the unpaid settlement amount, premium, deposit or margin call by the amount of the cash paid by the Counterparty or collateral held by the Trading Participant on behalf of the Counterparty if the collateral is liquid, valued at the mark to market value or another value approved by **CMIC** and the collateral arrangement between the Trading Participant is evidenced in writing. The requirements of the next succeeding subsection (C) on Use of Collaterals shall apply.

iii. Computation of the Counterparty Risk Requirement on Margin Financing Lending shall be made in accordance with Schedule B.5 of SEC Memorandum Circular No. 16 series of 2004 and Subsection A.6.b.1 above.

c. Use of Collateral to Reduce Counterparty Risk Exposure

c.1. A Trading Participant may reduce its Counterparty Risk Exposure that serves as the basis in the computation of Counterparty Risk Requirement if sufficient collateral or security is available to cover the exposure. For purposes of determining whether the security is properly collateralized, the criteria prescribed under the provision on the computation of net liquid capital shall be used, in so far as they are applicable.

c.2. The value of the collateral used to reduce Counterparty Risk Exposure shall be net of the appropriate Position Risk Requirements as set forth in A.5.

c.3. The Commission may in the future provide additional guidelines or directives relating to the discounting of collaterals.

c.4. Reconciliation and inventory counts, when appropriate, should be done on all collaterals at month end.

A.7 Large Exposure Risk Requirement (LERR).

a. General Principles.

a.1. A Member Company shall compute its Large Exposure Risk Requirement in relation to -

- i. its exposure to a single client or counterparty;
- ii. its direct exposure to debt; and
- iii. its direct exposure to a single equity and its group of companies;

for all amounts arising in the normal course of trading in equity and debt securities in accordance with the provisions set out under this Subsection A.7.

a.2 LERR shall be computed on counterparty transactions (for its exposure to a single client or counterparty) and proprietary positions (for its direct exposure to debt and single equity/issue or group of companies). For this purpose, the Counterparty Risk and Position Risk Requirements as prescribed in Subsections A.6 and A.5, respectively, shall be considered.

a.3 For purposes of computing the LERR for direct exposures to debt and single equity/issue or group, the position risk requirements of both securities held in proprietary accounts and as collateral of counterparties shall be aggregated.

a.4 The Commission may, upon written recommendation from **CMIC** reduce or waive the Large Exposure Risk Requirement for specific Trading Participants subject to terms and conditions as the Commission deems fit. The Commission may also reduce, increase, vary or waive the maximum Large Exposure Risk prescribed in this subsection as the Commission deems fit.

b. Computation of LERR

b.1. Exposure to a single client/counterparty

i. A Large Exposure Risk to a single client/counterparty occurs when the total of the Counterparty Risk Requirement for such single client/counterparty as computed in Subsection A.6 (b) above exceeds ten percent (10%) of the Trading Participant's Core Equity.

ii. For purposes of computing the Trading Participant's Large Exposure Risk in relation to a single client or counterparty, the Trading Participant shall include its exposure to persons connected to that client or counterparty.

iii. The LERR of a Trading Participant to a single client or counterparty shall be equal to 100% of that portion of the counterparty risk exposure in excess of 10% of the Trading Participant's Core Equity.

iv. For purposes of this section, the term "single client or counterparty" includes -

(a) where such single client or counterparty is an individual, the individual, spouse of the individual, the partnership of which he is a partner, any partner of the individual, the spouse of the partner and all the companies or corporations over which the individual exercises control. For the purpose of this subsection, an individual is deemed to exercise "control" over a company or corporation if the individual or the individual's spouse, severally or jointly -

(aa) holds, directly or indirectly, more than fifty percent (50%) of the shares of the corporation,

(bb) has the power to appoint, or cause to be appointed, a majority of the directors of the company or corporation, or

(cc) has the power to make, cause to be made, decisions in respect of the business or administration of the company or corporation, and to give effect to such decisions, or cause them to be given effect to.

(b) where such single client or counterparty is a corporation, the corporation and its affiliated company where

the company exercises management and ownership control or significant control over the corporation.

v. The maximum LERR that a Trading Participant is allowed to carry in its books in relation to any single client or counterparty is thirty percent (30%) of its Core Equity.

vi. The Trading Participant shall report to **CMIC**/Commission promptly all its Large exposure risk relating to a particular client or counterparty. Reporting of write off of receivables of clients shall be governed by the provisions of Part 2.4 of these Rules.

b2. Direct Exposure to a debt issue

i. A Large Exposure Risk to a single debt issue when the Large Exposure Risk in relation to an issuer of debt as computed in Subsection A.5 (b) exceeds ten percent (10%) of the Trading Participant's Core Equity.

ii. The LERR of a Trading Participant to a single debt issue shall be equal to 100% of that portion of the net position or exposure in excess of 10% of the Trading Participant's Core Equity.

iii. The maximum LERR that a Trading Participant is allowed to carry in its books in relation to any single client or counterparty is thirty percent (30%) of its Core Equity.

iv. The Trading Participant shall report to **CMIC**/Commission promptly all its Large exposure risk relating to debt.

b.3 Direct exposure to a single equity relative to a particular issuer company and its group of companies;

i. A Large Exposure Risk to a single equity relative to a particular issuer and its group of companies happens when -

(a) LERR to Equity vs. Issuer Limit – It has a net position or exposure (either long or short) that exceeds five percent (5%) of the total listed issue of the equity **or market capitalization**; or

(b) LERR to Equity vs. Core Equity Limit – It has a net position or exposure that exceeds ten percent (10%) of the Trading Participant's Core Equity.

- ii. For purposes of determining what constitutes net position or exposure, the Trading Participant shall:
 - (a) Include underwriting and sub-underwriting agreements which are carried as principal positions of the Trading Participant;
 - (b) Include equity OTC options or equity warrants that are in the money at its full underlying value;
 - (c) Not treat out of the money equity OTC options or equity warrants as an exposure;
 - (d) Consider as part of single equity, positions held in other listed securities of affiliates.
- iii. For purposes of this section, single equity relative to a particular issuer and its group of companies, shall include:
 - (a) Collateral underlying debtors or margin accounts (including interest);
 - (b) Collateral underlying loans and advances; and
 - (c) Investment in the stock accounts; and
 - (f) Other securities of a similar nature.
- iv. Computation of the LERR to Equity vs. Issuer limit.
 - (a) The Trading Participant has to multiply the value of the exposure in excess of five percent (5%) of the total issue **or market capitalization** by the Position Risk Factor.
 - (b) A Trading Participant who has an exposure of twenty percent (20%) or more of the issuer's capital shall be assumed to exercise significant influence or control over the issuer company and accordingly such investment shall not be considered part of NLC and accordingly, is not included in the computation of LERR.
- v. Computation of LERR to Equity vs. Core Equity limit
 - (a) A Large Exposure Risk Requirement to a single equity is computed by multiplying the value of the exposure in excess of ten percent (10%) of the

Trading Participant's Core Equity by the Position Risk Factor as described in Subsection A.5 (a)

vi. In cases where LERR to Equity is computed for both Issuer and Core Equity limits, the higher of the two values shall be chosen to represent the Trading Participant's LERR for that particular Equity.

vii. The maximum LERR that a Trading Participant is allowed to carry in its books in relation to any equity is two hundred fifty percent (250%) of its Core Equity.

viii. The Trading Participant shall report to **CMIC**/Commission promptly all its Large exposure risk relating to debt.

B. SUBORDINATION AGREEMENTS

Section 1. All existing Subordination Agreements shall be considered part of the Net Capital/RBCA of relevant Trading Participants in accordance with the following schedule:

| Period remaining from RBCA Computation date to maturity date | Allowable Inclusion |
|--|------------------------|
| ----- | ----- |
| 3 years 1 day to 4 years | 100% |
| 2 years 1 day to 3 years | 75% |
| 1 year 1 day to 2 years | 50% |
| 1 year or less | 0% |

C. MINIMUM PAID-UP CAPITAL REQUIREMENT

Section 1. The unimpaired paid-up capital requirement is One Hundred Million Pesos (Php100,000,000.00) for the following types of Trading Participants:

(a) First time registrants who will be participating in a registered clearing agency upon the effectivity of the Code;

(b) Those acquiring the business of existing Trading Participants pursuant to SRC Rule 28.1, paragraph 2 and will be participating in a registered clearing agency;

Provided, however, that the Commission may authorize a lower capitalization for applicants not participating in a registered clearing agency.

Section 2. Other existing Trading Participants not meeting the One Hundred Million Pesos (Php100,000,000.00) capitalization and not seeking authorization to engage in market making transactions shall maintain Ten Million Pesos (Php10,000,000.00) unimpaired paid-up capital and file the required surety bond in lieu of the One Hundred Million Pesos as prescribed under SRC Rule 28.1 (5): Provided, that (a) the minimum unimpaired paid-up capital of these Trading Participants shall be Twenty Million Pesos (Php20,000,000.00) effective December 31, 2009 and Thirty Million Pesos (Php30,000,000.00) effective December 31, 2010: Provided further, that effective November 1, 2009, the surety bonds for brokers shall be Ten Million Pesos (Php10,000,000.00) and Two Million Pesos (Php2,000,000.00) for dealers.

Section 3. Unimpaired paid up capital of Two Million Five Hundred Thousand Pesos (Php2,500,000.00) for applicants dealing purely in proprietary shares and who are not holding securities.

ARTICLE IX. BOOKS AND RECORDS RULE

Section 1. *Books and Records Rule.* In addition to the requirements of the Books and Records Rule under SRC Rule 52.1, a Trading Participant shall make, keep current and maintain in its principal office the following books and records relating to its business:

(a) **Blotter and Similar Records** – A Trading Participant shall have blotters or books of original entry containing a historical account of all the daily transactions of the Trading Participant or its customers. The Trading Participant may keep a number of different blotters to record separate types of transactions, provided that the Trading Participants shall have at least:

(i) A Purchase and Sales Blotter setting forth for each transaction the purchaser and seller, subject security, certificate numbers or for uncertificated securities, equivalent identification numbers or location, quantity, price, amount, any interest or commission, trade date, and settlement date;

(ii) An IN/OUT Receipts Book setting forth the receipt and delivery of securities to and from customers, including information on the date of receipt or delivery of the securities to or from customers, name of security, number of shares, and whether the certificate was transferred to or from another Trading Participant or a name certificate will be lodged or uplifted; and

(iii) Cash Receipts/Disbursement Book setting forth the receipt and disbursement of cash, including information on the official receipt/check voucher number, check number, bank account wherein cash was withdrawn or deposited, utilization of the cash and accounting entries at the end of each month.

(b) **General Ledger** – A Trading Participant shall have a General Ledger reflecting all its assets and liabilities, and its income and expense and capital accounts, and from which a trial balance can be abstracted in order to prepare financial statements showing the Trading Participant's financial condition.

(c) **Customer's Ledger** – A Trading Participant shall have a Customer's Ledger, which shall set forth the itemized account activity and the securities positions and money balances of the customer. A complete set of the statements of account of a customer on file with the Trading Participant can be the Customer's Ledger.

(d) **Detailed Collateral Valuation Schedule** – A Trading Participant shall have a Detailed Collateral Valuation Schedule, which shall set forth the name of the customer, money balance, name of security, number of shares, market value of position, and percentage of total market value of position of customer over money balance classified as follows:

- (i) More than 250%;
- (ii) At least 200% but not more than 250%;

- (iii) At least 150% but not more than 200%;
- (iv) At least 100% but not more than 150%;
- (v) Less than 100%; and
- (vi) Fully Secured.

(e) Securities In Transfer Ledger – A Trading Participant shall have a Securities In Transfer Ledger, which shall show the number of the transfer receipts received from the transfer agent, the number of shares, name of security, name of previous owner, name of new owner, date sent out to transfer agent, old certificate number, date received back from transfer, and new certificate number.

(f) Dividends and Interest Received Ledger – A Trading Participant shall have a Dividends and Interest Received Ledger, which shall show the name of the security, the ex-dividend date (or interest date), the rate per share, and the payment date.

(g) Securities Borrowed and Securities Loaned Record – A Trading Participant shall have a record of securities borrowed to make deliveries against sales and securities lent to other Trading Participants. Said record shall state the borrowing or lending date, name of borrowing or lending Trading Participant, number of shares, name of security, price, amount, the date returned, and any interest or other compensation. As securities are marked to market, resulting in additional monies paid or collected, the record should reflect that money movement in order to balance the daily cash blotter and reflect the appropriate money amount to be paid or collected when the loan is paid.

(h) Record of Monies Borrowed, Monies Loaned, Etc. – A Trading Participant shall have a record of all borrowings, regardless of whether customers' or its securities are pledged as collateral. This record should show the name of the bank, the date of payment, and particulars of the collateral, if any.

(i) Record of Securities and Monies Failed to Receive or Failed to Deliver – A Trading Participant shall have a record of securities and monies, which the Trading Participant failed to receive or deliver. In case of failure to receive securities and monies, the Trading Participant shall state in said record the date on which delivery was due but not made, number of securities or amount of money, name of security, purchase price, Trading Participant from whom delivery is due, and date received. In case of failure to deliver securities and monies, the Trading Participant shall state in said record the date on which delivery was due, number of shares or amount of money, name of security, Trading Participant to whom securities were sold, sales price and date on which delivery is made.

(j) Securities Record or Ledger – A Trading Participant shall have securities record or ledger or position book, which shall state separately for each security all long or short positions (including securities in safekeeping) carried by the Trading Participant either for its account or for the account of its customers. Said record or ledger shall state the location of all securities "long," the offsetting position to all securities "short," and in all cases the name or designation of the account in which each position is carried.

(k) Order Ticket – A Trading Participant shall have a memorandum of each order and any other instruction, which the Trading Participant, on its behalf or on behalf of

its customer, gave or received for the purchase or sale of securities, whether executed or unexecuted. The memorandum shall state the terms and conditions of the order or instructions and of any modification or cancellation thereof, the account for which entered, the time of entry (*i.e.*, the time the order was transmitted by the Trading Participant and received by the relevant party), the price at which executed, and, to the extent feasible, the time of execution or cancellation. Orders entered pursuant to the exercise of discretionary power by the Trading Participant shall be so designated. A Trading Participant may adopt an electronic form for the order ticket with the approval of the Commission.

(l) Confirmations and Notices – A Trading Participant shall have copies of (i) confirmations of all purchases and sales of securities and (ii) copies of notifications of all other debits and credits for cash securities for the account of customers.

(m) Records on Cash and Margin Accounts – A Trading Participant shall have, in respect of each cash and margin account, a record containing the name and address of the beneficial owner of the account, and, in the case of a margin account, the signature of the owner, subject to the following rules:

(i) In case of a joint account or an account of a corporation, the record shall only be in respect of the person or persons authorized to transact business for such account;

(ii) In case of a Done Through Account, only the Trading Participant maintaining said account with another Trading Participant shall be regarded as the beneficial owner; the customers of the Trading Participant maintaining the account shall not be customers of the Trading Participant with whom the Done Through Account is maintained; and

(iii) Where a trustee, nominee or other fiduciary opens and maintains an account with a Trading Participant as a representative of one or more particular beneficiaries and where all transactions effected in that trust are solely for the particular predetermined beneficiaries for whom the account is maintained, such beneficiaries (who thus have ownership of the account itself as distinguished from an interest in particular securities or credits which may happen to be recorded therein) shall be beneficial owners of the account. Where the agent's or trustee's transactions on behalf of a trust or particular individuals are of such volume and importance as to warrant the opening of a separate account for the particular trust or individuals, the Trading Participant shall obtain the name and address either of the particular trust or of the beneficiaries.

(n) Monthly Trial Balances and Net Capital Computation – A Trading Participant shall prepare at least once a month a current record of (i) the proof of money balances in all ledger accounts in the form of trial balances and (ii) the computations of the aggregate indebtedness and net capital as of the trial balance date; Provided, however, that the computation of the aggregate indebtedness and net capital shall be made on a daily basis and available for review when requested by the Commission or **CMIC**.

(o) Employment Applications – A Trading Participant shall have on file an employment questionnaire or application for each Associated Person and Salesman. Said questionnaire or application shall state material information on such person, and must be approved in writing by the designated Associated Person or other authorized agent of the Trading Participant. A Trading Participant may comply with this record requirement by retaining a complete copy of the registration application, which the Trading Participant filed on behalf of such person with the Commission.

With the prior approval of the Commission and in addition to the computerized and effective recording and accounting system mandated by SRC 28.1(1)(E)(2)(x), a Trading Participant may make, keep current and maintain the books and records required by this Article IX and SRC Rule 52.1 in electronic form and/or medium (including electronic records, which the Exchange trading system may allow to be so made, kept current and maintained), provided that upon request by the Commission, **CMIC**, or any other party, who may be legally entitled or authorized to access said books and records, the Trading Participant shall promptly and readily provide a comprehensible and certified true printed and/or electronic copy of the books and records or any part thereof.

Section 2. *Accounting Standards.* All Trading Participants shall comply with the International Accounting Standards (IAS) and the Philippine Financial Reporting Standards as issued by the Board of International Accounting Standards Council.

Section 3. *Annual Audited Financial Reports of Trading Participants.* (a) Every Trading Participant shall file annually with the Commission and **CMIC** at the close of its fiscal year an audited financial report by an independent certified public accountant and a statement of management responsibility of said Trading Participant.

(b) Unless the Trading Participant notifies the Commission otherwise and receives written approval to change the date, December 31st of each year shall be considered the closing of the fiscal year, and the Annual Audited Financial Report is due within 110 days after the close of such fiscal year. **This should be without prejudice to the authority of the Commission to provide for a different date for the submission of the Annual Audited Financial Report, in which case, the Annual Audited Financial Report may be submitted to CMIC on the same date.**

(c) The Annual Audited Financial Report shall contain a Statement of Financial Condition in the format outlined in Commission Form 37-AR, a Statement of Income, a Statement of Changes in Financial Condition, a Statement of Changes in Stockholders' or Partners' or Sole Proprietor's Equity, a Statement of Changes in Liabilities Subordinated to Claims of General Creditors, a Computation of Net Capital under SRC Rule 49.1-1, Statement of Management's Responsibility; Information relating to the Possession or Control Requirements under Annex F of SRC Rule 49.2-1 and a Computation for Determination of Reserve Requirements under Annex G of SRC Rule 49.2-1; Report describing any material inadequacies found to exist or found to have existed since the date of the previous audit; Results of **Monthly** Securities Count Conducted pursuant to SRC Rule 52.1-10 as of the date of the balance sheet statement in the Annual Audited Financial Report.

(d) All supporting papers pertaining to such report or statement shall be kept in the possession of the Trading Participant for at least five (5) years and shall be made available for examination by the Commission and **CMIC**.

(e) For the purposes of this Rule, the term market value shall be understood to mean the last sale price of the security on the date of the report or statement; if no sale of the corresponding security is made on that date, it shall be understood to mean the bid price and, in the absence of any buyer, it shall be taken to mean the last sale price which is below the offer price on the date of the report or statement. For purposes of determining "market value" for a short position, where no sale of the corresponding security is made on that date, it shall be understood to mean the offer price and, in the absence of any seller, it shall be taken to mean the last sale price which is above the bid price on the date of the report or statement.

(f) For the purposes of this Rule, the term material inadequacy encompasses either a material weakness in internal control or a material inadequacy in the practices and procedures for safeguarding securities. A material inadequacy that is expected to be reported includes any condition that has either contributed substantially to or, if appropriate corrective action is not taken, could reasonably be expected to cause any of the following:

(i) Inhibit a Trading Participant from completing securities transactions or promptly discharging its responsibilities to customers or to other Trading Participants or creditors;

(ii) Result in material financial loss;

(iii) Result in material misstatements of the Trading Participant's financial statements;

(iv) Result in violations of the Commission's recordkeeping or financial responsibility rules to an extent that could reasonably be expected to result in the conditions described above.

If conditions believed to be material weaknesses are found to exist or have existed during the year, the report should disclose the nature of the weaknesses and the corrective action taken or proposed to be taken by the Trading Participant. If management has implemented control procedures to correct the weaknesses, the auditor should not refer to this corrective action in his or her report unless the auditor is satisfied that the procedures are suitably designed to correct the weakness and are being applied as prescribed.

ARTICLE X. RULES ON SUSPENSION OF TRADING OPERATIONS

Section 1. *Suspension of Trading Operations.* Suspension of trading operations may either be voluntary or involuntary. In voluntary suspension, the Trading Participant applies for the suspension of its trading operations. In involuntary suspension, **CMIC** or the Commission initiates and orders the suspension of the trading operations of the Trading Participant in accordance with the Securities Laws.

Section 2. *Requirements and Filing of Application for Voluntary Suspension.* A Trading Participant (the "Applicant") seeking to voluntarily suspend its trading operations shall file with CMIC, with a copy furnished to the Commission, an application for voluntary suspension ("application"), at least thirty (30) days prior to the intended date of cessation of trading operations. The application must be verified by the President or the Nominee, the Associated Person or the equivalent officer of the Applicant pursuant to Section 9, Article I of these Rules and must state:

- (a) the name and address of the Applicant;
- (b) the reasons and causes of the application for voluntary suspension;
- (c) a summary of the Applicant's liabilities to customers;
- (d) a summary of the Applicant's trade-related assets and their balances and market values. Trade-related assets are the assets of the Trading Participant that are necessary before it may trade, or are used to promote its trading activities or have otherwise acquired the characteristic as trade-related by virtue of regulation of the Commission, such as, trading rights, reserve requirement, PSE shares and other similar assets;
- (e) its proposal for at least three (3) "Successor Trading Participants" to take over all its contracts and transactions with, and accounts of, customers, subject to CMIC approval; and
- (f) that it was duly authorized to file application by the board of directors, stockholders and/or other governing body of the Applicant.

The Applicant shall attach as integral parts of the application, the following documents:

- (a) the audited financial statements of the Applicant as of the end of its last fiscal year;
- (b) the interim financial statements of the Applicant at least as of the end of the month prior to the filing of the application;

(c) the schedule of the Applicant's debts and liabilities to customers, which shall list all the customers of the Applicant, indicating the name and address of each customer, the amount of each claim as to principal, interest, or penalties due as of the date of filing of the application, and any pledge, lien, mortgage, or other security given for the payment thereof;

(d) the inventory of the Applicant's trade-related assets, which shall particularly list all the trade-related assets of the Applicant, stating the nature, location, condition (including any claim, lien or encumbrance), book or market value, and certificate or evidence of title or ownership of each asset;

(e) a certificate of the Applicant's corporate secretary or other relevant authority attesting, under oath, that the board of directors, stockholders, and/or other person or body governing the Applicant has duly authorized the filing of the application; and

(f) The undertaking of the Applicant as set forth in Section 3 of this Article IX.

Section 3. *Undertaking of Applicant for Voluntary Suspension.* The Applicant shall file, together with the application, an undertaking under oath with the following terms and conditions:

(a) The Applicant shall pay all its trade-related liabilities and obligations prior to the date of effectivity of the voluntary suspension;

(b) It shall cease to solicit new clients upon filing of the application for voluntary suspension;

(c) It shall cease to execute any order of customers at least five (5) days prior to the intended date of cessation of trading operations as set forth in the application for voluntary suspension;

(d) It shall maintain its surety bond until its expiration;

(e) It shall not transfer to the Successor Trading Participant or otherwise dispose of the securities of its customers without their prior written agreement;

(f) It shall continually inform the customers of its transactions and activities until the complete transfer of the customers' accounts to the Successor Trading Participant;

(g) It shall notify all customers of the application for voluntary suspension, the intended date of cessation of its trading operations, and the approved Successor Trading Participant. It shall obtain from the client a written agreement for the transfer of their account to the Successor Trading Participant, or in the alternative, their broker of choice;

(h) It shall preserve and maintain for a period of not less than five (5) years from the date of the approval by **CMIC and/or** the Exchange of the application for voluntary suspension all records required to be preserved and/or maintained pursuant to the Securities Laws. It shall promptly inform **CMIC** and the Commission of the names, residential addresses, and contact numbers of at least two (2) persons responsible for the safekeeping of said records, and any change in said persons. If money laundering, criminal, administrative or other investigations, cases or other proceedings involving a customer of the Applicant have been commenced in court or any governmental agency, the Applicant shall preserve and maintain the relevant records until the final resolution of the investigations, cases or other proceedings by the court or any governmental agency;

(i) It shall comply with all specific measures, which **CMIC** may adopt to protect the interest of its customers, the Exchange, and other Trading Participants. For this purpose, it shall irrevocably appoint CMIC and/or any of its agents as the Applicant's attorney-in-fact with full power and authority to execute any and all acts necessary or appropriate to comply with said measures, including the power and authority to take possession and control of, and liquidate all trade-related assets of the Applicant to settle its liabilities to customers pursuant to the Securities Laws;

(j) It shall cause its President or the equivalent officer or Associated Person to oversee and ensure its compliance with all the requirements of the Commission and/or **CMIC** relative to the voluntary suspension of trading operations; and

(k) It shall pay all costs and expenses which **CMIC** may incur in connection with, or arising out of, its application for voluntary suspension.

Section 4. *Consequences of Application for Voluntary Suspension.* CMIC shall undertake the following actions in connection with the application for voluntary suspension of the Applicant, which the Applicant, by filing the application for voluntary suspension, shall be deemed to have agreed to:

(a) Special Audit of the Applicant. Upon its receipt of the application for voluntary suspension from the Applicant, CMIC shall conduct a special audit of the Applicant. CMIC shall focus the audit on the existence and valuation of the Applicant's trade-related assets on record and its trade-related liabilities or its obligations to customers, the clearing house, the Exchange, the depository, and other Trading Participants. CMIC shall exert best efforts to complete the special audit in fifteen (15) days, and come up with its Examination Findings and recommended measures and other actions to protect the interests of the customers, the clearing house, the Exchange, and other Trading Participants in relation to the Applicant and the application for voluntary suspension.

(b) Suspension of Access to the Exchange's Trading System. On the date of the effectivity of the voluntary suspension, the PSE shall deactivate the Applicant's access to the Exchange's trading system.

(c) Freezing of the Account with the Clearing Agency and the depository. CMIC shall issue instructions to the Clearing Agency to disallow, beginning on the date of the effectivity of the voluntary suspension, the delivery and/or over-the-counter clearing of securities and stock assignments of any security in the name of the Applicant without the prior written approval of CMIC. CMIC shall also instruct the depository (a) to deny the Applicant, beginning on the date of the effectivity of the voluntary suspension, any access to the Depository Online System and (b) to transfer all accounts of the Applicant to the account, which CMIC shall establish and maintain for the purpose.

(d) Notice to the Commission and Other Trading Participants. On or before the effectivity of the voluntary suspension, CMIC shall notify in writing, the Commission and all Trading Participants of the approval of the voluntary suspension of the Applicant. CMIC shall direct all Trading Participants to inform CMIC, on or before said effectivity date, of all their pending transactions and contracts with the Applicant.

(e) Notice to Customers. CMIC shall notify the customers of the voluntary suspension of the Applicant by (i) publishing once a week for three consecutive weeks in a newspaper of general circulation in Metro Manila and (ii) posting on the Exchange and **CMIC** websites the notice of voluntary suspension of the Applicant. The notice shall:

(i) state the fact of the voluntary suspension of the Applicant;
and

(ii) state other directives or information as may be ordered by the Commission or CMIC, or as may be agreed upon with the Applicant.

(f) Reports and Disposition of Assets. During the period of its voluntary suspension not involving complete cessation of trading operations or closure of business and unless otherwise directed by CMIC, the Applicant shall be exempted from the reporting obligation of Trading Participants under these Rules. However, the Applicant shall not dispose of or encumber its assets without the written approval of CMIC.

Section 5. *Approval of Voluntary Suspension.* Should CMIC determine that (a) the Applicant has complied with all the requirements herein and (b) the interests of the customers, the Exchange, the clearing house, and other Trading Participants are adequately protected, CMIC shall approve the voluntary suspension. Otherwise, CMIC shall take such actions necessary or appropriate to safeguard the interests of the customers, the Exchange, the clearing house, and other Trading Participants in relation to the Applicant, including the involuntary suspension of the Applicant as provided in this Article X.

Section 6. *Resumption of Operations.* With the approval of CMIC and the Commission, a Trading Participant under voluntary suspension, which does not involve a complete cessation of trading operations or closure of business, may resume trading operations by securing a secondary license from the Commission and complying with the Risk Based Capital Adequacy Rule and Minimum Unimpaired Paid-up Capital Requirement as provided in Article VIII: Capitalization Requirement and other relevant requirements of the Securities Laws.

Section 7. *Grounds for Involuntary Suspension.* CMIC may place a Trading Participant under involuntary suspension in any of the following cases:

(a) The Commission orders **CMIC** to take over the operations of a Trading Participant in accordance with SRC Rule No. 33.2(d);

(b) An Applicant for voluntary suspension violates any of its undertakings under Section 3 of Article **X**, especially the payment of all its trade-related liabilities and obligations prior to the date of effectivity of the voluntary suspension;

(c) The Trading Participant has been suspended for the third time in one (1) year for failure to settle its obligation/s to the clearing house;

(d) The Trading Participant has been suspended by the Clearing Agency from availing of the clearing house facilities pursuant to the Clearing Agency's rules; and

(e) The Trading Participant failed to improve its RBCA ratio and Net Liquid Capital (NLC) within the period as prescribed by the CMIC, after breaching the minimum RBCA ratio of 1.1 and minimum NLC of five (5) million pesos.

(f) The Trading Participant failed to meet the required unimpaired paid-up capital as required under the SRC Rule 28.1 (E).

(g) The Trading Participant failed to maintain a sufficient number of personnel, including but not limited to, the licensed trader and Associated Person.

(h) When CMIC has determined that the continued operation of the Trading Participant constitutes a grave violation of the Securities Laws and is inimical to the interest of the Exchange, the investors and the public in general.

Section 8. *Procedure for Involuntary Suspension.* (a) Should CMIC determine that the financial condition of a Trading Participant has so deteriorated that it cannot readily meet the demands of its customers for the delivery of securities and/or the payment of sales proceeds, CMIC shall file with the Commission a petition for the Commission to authorize CMIC to take over the operations of said Trading Participant pursuant to SRC Rule 33.2(d). In such case, the involuntary suspension of the Trading

Participant pursuant to a take-over order under SRC Rule No. 33.2(d) shall be governed primarily by said take-over order and relevant provisions of the Securities Laws, and suppletorily by these Rules.

(b) In all other cases of involuntary suspension, CMIC shall substantially follow the applicable provisions of Article II of these Rules in deciding whether to place a Trading Participant under involuntary suspension.

Section 9. *Consequences of Involuntary Suspension of a Trading Participant.* Upon the involuntary suspension of a Trading Participant (the "Suspended TP"), CMIC shall undertake the following actions:

(a) Takeover of the Books and Records and Trade-related Assets of the Suspended TP. With the approval of the Commission or with the agreement of the Suspended TP, CMIC shall:

- (i) Immediately take possession and control of all books and records and trade-related assets of the Suspended TP;
- (ii) Retain custody over these books, records and trade-related assets for a period of not less than five (5) years, from the date that the Commission issued the takeover order. If administrative, civil or criminal cases have been filed in court or an investigation is being conducted on the Broker Dealer involved or impleaded as a party to the case or investigation, **CMIC** shall retain custody over these books, records and trade-related assets which must be retained beyond the five (5) year period until it is confirmed by final judgment that the case has been finally resolved or terminated.
- (iii)** Liquidate the trade-related assets of the Suspended TP and pay its liabilities to customers and other trade-related liabilities; and
- (iv)** Take such action as may be ordered by the Commission or CMIC Head, or as may be agreed upon with the Suspended TP.

(b) Special Audit of the Suspended TP. CMIC shall conduct a special audit of the Suspended TP. CMIC shall focus the audit on the Suspended TP's trade-related liabilities or its obligations to customers, the clearing house, the Exchange, and other Trading Participants. CMIC shall exert best efforts to complete the special audit in fifteen (15) days, and come up with its Examination Findings and recommend measures and other actions to protect the interests of the customers, the clearing house, the Exchange, and other Trading Participants in relation to the involuntary suspension of the Suspended TP.

(c) Suspension of Trading Right and Access to the Exchange's Trading System. The involuntary suspension of a Trading Participant shall automatically result in the suspension of its Trading Right. On the date of the effectivity of the involuntary

suspension, the ITD shall deactivate the Suspended TP's access to the Exchange's trading system.

(d) Freezing of Account with the Clearing Agency and the depository. CMIC shall issue instructions to the Clearing Agency to disallow, beginning on the date of the effectivity of the involuntary suspension, the delivery and/or over-the-counter clearing of securities and stock assignments of any security in the name of the Suspended TP without the prior written approval of CMIC. CMIC shall also instruct the depository to deny the Suspended TP, beginning on the date of the effectivity of the involuntary suspension, any access of the Suspended TP to the Depository Online System.

(e) Notice to the Commission and Other Trading Participants. CMIC shall notify in writing the Commission and all Trading Participants of the involuntary suspension of the Suspended TP. CMIC shall direct all Trading Participants to inform CMIC of all their pending transactions and contracts with the Suspended TP.

(f) Notice to Customers. CMIC shall notify the customers of the Suspended TP of its involuntary suspension by (i) publishing once a week for three consecutive weeks in a newspaper of general circulation in Metro Manila and (ii) posting on the Exchange and **CMIC** websites the notice of involuntary suspension of the Suspended TP. The notice shall:

- (i) state the fact of the involuntary suspension of the Suspended TP;
- (ii) direct each customer of the Suspended TP to file with CMIC a notarized affidavit of claim with attached certified photocopies of (a) two (2) valid identification cards of the claimant and (b) documents supporting the claim within thirty (30) days from the date of the first publication of the notice;
- (iii) inform customers of the Suspended TP that they may also claim compensation for losses from the SIPF and the surety bond of the Suspended TP; and
- (iv) state other directives or information as may be ordered by the Commission or CMIC, or as may be agreed upon with the Suspended TP, including the transfer of customers' accounts to a Successor Trading Participant.

Section 10. *Validation of Claims.* CMIC shall validate claims of customers against a Trading Participant under voluntary or involuntary suspension in accordance with the following rules:

(a) CMIC shall require each customer with a claim against a suspended Trading Participant to file with CMIC:

- (i) A duly accomplished Claim Processing Sheet prescribed by CMIC;
- and

(ii) A notarized affidavit of claim with the following certified attachments:

(1) Photocopies of documents supporting the claim (e.g., statements of accounts, confirmation invoices, customers ledgers, official receipts, checks and check vouchers, or other documents given by the trading participant); and

(2) Photocopies of any two (2) valid identification cards (e.g., TIN card, SSS/GSIS card, PRC card, driver's license, passport, and company ID).

If an agent will file the claim for and on behalf of the customer, the agent should submit the following additional documents:

(i) Proof of authority of the agent to act for and on behalf of the customer; and

(ii) Certified photocopies of any two (2) valid identification cards of the agent.

(b) CMIC shall validate all claims filed against, and other trade-related liabilities of, the suspended Trading Participant based on (i) the documents submitted by the customers, (ii) the books and records of the suspended Trading Participant, and (iii) other documents and records available to CMIC.

(c) CMIC shall fix the value of the claims as of the date of the effectivity of the voluntary or involuntary suspension.

(d) Upon completion of the validation of the claims, CMIC shall submit to the Commission for its comment and approval a report on the results of the validation of the claims. Before filing said report, CMIC shall (i) furnish a copy thereof to the suspended Trading Participant and (ii) with respect to each claim filed against the Trading Participant, notify the relevant customer in writing of the result of the validation of said customer's claim.

Section 11. *Settlement of Claims.* (a) Upon approval by the Commission of the validated claims of customers, CMIC shall prepare and submit to the Commission for its approval a plan for the allocation and liquidation of the trade-related assets of a suspended Trading Participant in accordance with the following order of allocation:

(i) Costs and expenses incurred by **CMIC** in accordance with Section 12 of this Article;

(ii) CMIC shall set aside securities in the name of a specific customer in favor of said customer;

(iii) CMIC shall set aside the securities or amounts necessary to pay the costs of the voluntary or involuntary suspension, including the liquidation of the trade-related assets of the suspended Trading Participant to pay its liabilities to customers and other trade-related liabilities;

(iv) CMIC shall set aside for the benefit of the SIPF securities or amounts pertaining to validated claims already paid by the SIPF to relevant customers;

(v) With reference to each specific class of securities (the "Specific Securities") remaining after setting aside the securities as provided in paragraphs (i), (ii) and (iii) of this Section 11 (a), CMIC shall allocate the Specific Securities to customers with validated claims to the Specific Securities in the proportion that a customer's validated claim to the Specific Securities shall bear to all validated claims to the Specific Securities of all customers; and

(vi) CMIC shall allocate the remaining securities and trade-related assets of the suspended Trading Participant to customers with remaining validated claims for securities and/or cash in the proportion that the value of a customer's remaining validated claim shall bear to the aggregate value of all remaining validated claims of customers.

(b) Before filing said plan to the Commission, CMIC shall (i) furnish a copy thereof to the suspended Trading Participant and (ii) with respect to each claim filed against the Trading Participant, notify the relevant customer in writing of the trade-related assets of the suspended Trading Participant allocated to said customer.

(c) Upon approval by the Commission of a plan for the allocation and liquidation of the trade-related assets of a suspended Trading Participant, CMIC shall send notice of said approval to the suspended Trading Participant and its customers by (i) registered mail, (ii) publication of the notice at least once in a newspaper of general circulation, and (iii) posting on the PSE website.

(d) CMIC shall pay to the customer the trade-related assets of the suspended Trading Participant allocated to said customer under the approved plan only upon submission of the following documents:

(i) All documents previously submitted to and received by CMIC, including the original identification cards submitted;

(ii) Release, waiver and quit claim in favor of, and acceptable to, CMIC; and

(iii) Acknowledgment receipt for the trade-related assets received by the customer under the approved plan.

Section 12. *Costs and Expenses.* A Trading Participant under voluntary and involuntary suspension shall pay all costs and expenses, which **CMIC** may incur in connection with, or arising out of, the suspension of the Trading Participant.

ARTICLE XI. TRADING IRREGULARITIES

A. UNUSUAL TRADING ACTIVITIES

Section 1. *Responsibility of CMIC.* CMIC shall monitor daily the trading activity in the Exchange through its computer terminals to detect any Unusual Trading Activities or possible Trading-related Irregularities.

CMIC shall have the power and function to issue restriction, halt or suspension orders against trading of a listed security, or against trading by a Trading Participant of a particular listed security upon breach of pre-established price and/or volume benchmarks or when CMIC deems it necessary or appropriate under the circumstances.

Section 2. *Power to Restrict, Halt or Suspend Trading of a Listed Security or a Trading Participant.* CMIC may restrict, halt or suspend (a) the trading of a listed security of an Issuer or (b) the trading by a Trading Participant of a particular listed security in cases of Unusual Trading Activities or possible Trading-related Irregularities based on parameters established by CMIC pursuant to the Securities Laws.

Without prejudice to the other provisions of this Rules, CMIC, within a reasonable time upon its detection or suspicion of transactions constitutive of Unusual Trading Activities or Trading-Related Irregularities, shall require the Issuer and/or the Trading Participant, as the case may be, to explain the same in writing, and to submit the written explanation to CMIC not later than the time stated in its directive.

CMIC shall review the response of the Issuer and/or the Trading Participant, as the case may be. Should CMIC require further information, it may send a follow-up letter to the Issuer and/or the Trading Participant, and the latter shall respond to the same in accordance with the period and procedure set forth in this Section.

Should CMIC determine the existence of Unusual Trading Activities or Trading-Related Irregularities, CMIC shall decide the appropriate sanction/s to be imposed on the Issuer and/or Trading Participant, which may be in the form of a trading halt, suspension or trading restriction.

CMIC, through its President, shall inform the President of the Exchange in writing of the decision of CMIC, the disciplinary sanction/s imposed on the Issuer, and the period of effectivity of said sanction/s.

Section 3. *Lifting of Restriction, Halt or Suspension Order and Resumption of Trading of a Listed Security or Trading Participant.* A restriction, halt or suspension

order shall subsist until lifted by CMIC. CMIC shall lift a restriction, halt or suspension order only upon determination by CMIC of the adequacy of the information and disclosures provided by the relevant parties to explain the transactions constitutive of Unusual Trading Activities or possible Trading-related Irregularities. Even pending determination of the adequacy of the relevant information and disclosures, CMIC, with the concurrence of the President, may lift the restriction, halt or suspension order if the lifting will serve the best interests of the Exchange, the investors and the public in general.

Section 4. *Notice to the Commission.* CMIC shall notify the Commission by telephone or by facsimile (a) not later than fifteen (15) minutes after issuance of a restriction, halt or suspension order if the market is still in session or (b) not later than 4:00 p.m. of the same day if the order will take effect the following day. In both instances, CMIC shall deliver to the Commission the formal written notice not later than 11:00 a.m. of the next day.

Section 5. *Procedure for Issuance of Restriction, Halt or Suspension Orders.* Without limiting the powers of CMIC under Section 5, Article I and under Article II of these Rules, CMIC shall follow the procedures set forth below in deciding whether to restrict, halt or suspend (a) the trading of a listed security of an Issuer or (b) the trading by a Trading Participant of a particular listed security.

(a) As soon as CMIC shall have monitored transactions constitutive of Unusual Trading Activities or possible Trading-related Irregularities (including instances when the price of a listed security exceeds or closes at or near the ceiling or floor price based on the approved price trading band), CMIC shall verify with the Commission, the DD, and the Issuer whether the Issuer has made a previous disclosure that could have triggered said transactions.

(b) CMIC shall also direct the Issuer and, in case of restriction, halt or suspension of trading by a Trading Participant of a particular listed security, the relevant Trading Participant to submit, not later than 4:00 p.m. of the relevant day **for the morning trading session or 8:00 a.m. of the following day for the afternoon trading session**, a written statement confirming the existence or absence of any undisclosed information that could have triggered subject transactions. The written statement shall be under oath and signed by the President (and in case of a Trading Participant, its Associated Person), Corporate Secretary, Chief Information Officer, Compliance Officer or any duly authorized representative of the Issuer or the Trading Participant. CMIC may issue the directive verbally, provided that CMIC shall confirm the directive in writing either (i) by fax or email, provided the recipient acknowledges in writing receipt of the directive, or (ii) by personal delivery of the original thereof.

(c) If the Issuer or the relevant Trading Participant, as the case may be, does not comply with the directive, CMIC may, but is not obliged to issue a restriction, halt or suspension order in accordance with Section 2 of Article XI A.

If the Issuer or the relevant Trading Participant, as the case may be, complies with the directive by submitting a written statement, CMIC shall:

- (i) cause the circulation among Trading Participants and posting on the PSE website of the submitted written statement;
- (ii) if compliance was made after issuance of a restriction, halt or suspension order, decide whether to lift the order in accordance with Section 3 of Article XI A, provided that the lifting of the order shall take effect only not earlier than one (1) hour after circulation and posting of the written statement; and/or
- (iii) decide whether to issue a restriction, halt or suspension order in accordance with Section 2 of Article XI A.

B. TRADING-RELATED IRREGULARITIES

Section 1. *General Conduct.* In addition to the manipulative and fraudulent practices prohibited by the Securities Laws, a Trading Participant shall not:

- (a) Do any act or engage in any course of conduct which creates or is likely to create a false or misleading appearance as to the market in, or the price or value of, any listed security;
- (b) Cause a fictitious transaction or a false price to be inputted into the Exchange trading system;
- (c) Effect a transaction involving a listed security at any price which differs to an unreasonable extent from any firm price of said listed security displayed on the Exchange trading system;
- (d) Do any act or engage in any course of conduct which is likely to damage the fairness or integrity of the Exchange's markets;
- (e) Do any act or engage in any course of conduct whose sole or main purpose is to move the price of a listed security or the level of any index which includes said listed security as a component; or
- (f) Do any act or engage in any course of conduct which causes, or contributes to, a violation of the Exchange's/ CMIC's rules by another;
- (g) Simulate or make improper use of Subordination Agreement/s; and
- (h) Engage in the unauthorized use or disposition of funds or securities entrusted by a client to a Trading Participant in the course of its trading business;

(i) Engage in rogue algorithmic trading and other similar activities that may result in, but not limited to, irregular price movement of a particular security; and

(j) (i) Violate risk management and supervisory procedures set forth in pertinent rules on direct market access (“DMA”) or other alternative trading systems.

Section 2. *Obligation to Report Known or Suspected Violations.* Should a Trading Participant know or suspect a customer’s transaction to constitute Unusual Trading Activities, Trading-related Irregularities or any other violation of the Securities Laws, the Trading Participant shall report in writing to CMIC such knowledge or suspicion within twenty-four (24) hours from receipt of the customer’s order for the transaction. A Trading Participant shall be disputably presumed engaged in Unusual Trading Activities, Trading-related Irregularities or other violation of the Securities Laws if the Trading Participant fails to make said report to CMIC within the given period.

Section 3. *Insider Trading.* It shall be unlawful for an insider to sell or buy a security of the issuer, while in possession of material information with respect to the issuer or the security that is not generally available to the investing public.

Section 4. *Presumption of Possession of Material Information.* A purchase or sale of a security of the issuer made by an insider or such insider’s spouse or relatives by affinity or consanguinity within the second degree, legitimate or common-law, shall be presumed to have been effected while in possession of material non-public information if transacted after such information came into existence but prior to the dissemination of such information to the investing public and the lapse of a reasonable time for the market to absorb such information.

When an insider trades in possession of material non-public information, it is presumed that such information was used by the insider in trading.

This presumption, however, can be rebutted upon a showing by the insider that he was not aware of the material non-public information at the time of the purchase or sale.

Section 5. *Insider.* For purposes of this Article an insider means –

- (a) the issuer;
- (b) a director or officer (or person performing similar functions) of, or a person controlling the issuer;
- (c) a person whose relationship or former relationship to the issuer gives or gave him access to material information about the issuer or the security that is not generally available to the public;

(d) a government employee, or director, or officer of an exchange, clearing agency and/or self-regulatory organization who has access to material information about an issuer or a security that is not generally available to the public; or

(e) a person who learns such information by a communication from any of the foregoing insiders.

Section 6. *Material Information.* The information is considered material if:

(a) the information would likely affect the market price of the security after being disseminated to the public and the lapse of a reasonable time for the market to absorb the information, or

(b) a reasonable person would consider the information important under the circumstances in determining his course of action whether to buy, sell or hold a security in the light of such factors as the degree of its specificity, the extent of its difference from information generally available previously, and its nature and reliability.

Section 7. *Market Manipulation.* Market manipulation refers to the intentional interference with the free market forces of supply and demand designed to deceive or defraud investors (e.g., by giving the appearance of trading for the purpose of inducing others to either buy or sell).

Section 8. *Responsibilities by Trading Participants in Executing Orders to Avoid Market Manipulation.* It shall be unlawful for any Trading Participant, associated person or salesman of a Trading Participant (hereinafter collectively referred to as "Registered Person"), to make a bid or offer for, or deal in securities, for the account of the Registered Person or any other person where the Registered Person intends to create, or the Registered Person is aware that the other person intends to create, or taking into account the circumstances of the order, the Registered Person reasonably suspects that a person has placed the order with the intention of creating, a false or misleading appearance of active trading in any security or with respect to the market for, or the price of, any security or if that bid, offer or dealing, has the effect or is likely to have the effect, of creating a false or misleading appearance of active trading in any security or with respect to the market for, or the price of, any security.

If the Trading Participant reasonably suspects a violation of the preceding paragraph, the trading participant shall inform CMIC in writing of such possible violation within twenty-four (24) hours. Failure to notify CMIC shall raise the presumption that the Trading Participant is engaged in manipulative activity.

In considering whether an order violates Section 24 of the Securities Regulation Code, a Trading Participant shall consider:

(a) Whether the order, or execution of the order, would materially alter the market for, and/or the price of, the securities;

(b) The time the order is entered or any instructions concerning the time of entry of the order;

(c) Whether the person on whose behalf the order is placed, or another person who the Trading Participant knows to be a related party of that person, may have an interest in creating a false or misleading appearance of active trading in any security or with respect to the market for, or the price of, any security;

(d) Whether the order is accompanied by settlement, delivery or security arrangements which are unusual;

(e) Whether the order appears to be part of a series of orders, whether when put together with orders which appear to make up the series, the order or the series is unusual having regard to the matters referred to in this paragraph 3; and

(f) Whether there appears to be a legitimate commercial reason for that person placing the order, unrelated to an intention to create a false or misleading appearance of active trading in or with respect to the market for, or price of, any security.

Failure to consider these factors shall raise a presumption that a transaction/s is manipulative.

Obligations imposed on Registered Persons under this Rule apply in respect of all orders, irrespective of the trading system used.

Section 9. *Manipulative Schemes.* Set forth below are non-exclusive examples of types of prohibited conduct:

(a) Engaging in a series of transactions in securities that are reported publicly to give the impression of activity or price movement in a security (e.g. painting the tape);

(b) Posting actual or fictitious bid or offer at or near the close of the market, whether matched/executed or not, in an effort to alter or is likely to have the effect of altering the closing price of the security (marking the close);

(c) Engaging in transactions where both the buy and sell orders are entered at substantially the same time with the same price and quantity by different but colluding parties (improper matched orders);

(d) Engaging in buying activity at increasingly higher prices and then selling securities in the market at the higher prices (hype and dump);

(e) Engaging in transactions in which there is no genuine change in actual ownership of a security (wash sales);

(f) Taking advantage of a shortage of securities in the market by controlling the demand side and exploiting market congestion during such shortages in a way as to create artificial prices (squeezing the float);

(g) Disseminating false or misleading market information through media, including the internet, or any other means to move the price of a security in a direction that is favorable to a position held or a transaction.

Section 10. *Liability in Participating in Market Manipulations.* Any Trading Participant who willfully participates in any act or transaction in violation of the provisions of this Article shall be liable to any person who shall purchase or sell any security at a price resulting from such act or transaction, and the person so injured may sue in any court of competent jurisdiction to recover losses suffered as a result of any such act or transaction. The aggrieved person may avail himself of the remedy provided for in Section 59 of the SRC.

ARTICLE XII. DISCIPLINARY GUIDELINES AND SANCTIONS

Section 1. *Disciplinary Powers of CMIC.* CMIC shall have authority to discipline a Trading Participant, **or an Issuer in proper cases**, for violations of the Securities Laws or for acts or omissions inconsistent with just and equitable principles of fair trade, in accordance with these rules. To avoid any ambiguity on the application of this Article XII and unless the context requires otherwise, the term "Trading Participant" under this Article XII shall include directors, officers, Associated Person, Salesmen and other agents of a Trading Participant.

Section 2. *Purposes of Disciplinary Sanctions.* Disciplinary sanctions are remedial in nature and are designed to:

- (a) Ensure compliance by Trading Participants with applicable provisions of the Securities Laws;
- (b) Prevent fraudulent and manipulative acts and practices and deter misconduct of Trading Participants and in the proper case, Issuers;
- (c) Promote just and equitable principles of trade among market participants in general, and open and fair business practices among Trading Participants in particular; and
- (d) Improve overall business standards in the securities market.

Section 3. *Classification of Violations.* Violations of these rules and Securities Laws may be grave, major or minor.

- (a) The following are considered **major** violations:
 - (i) Simulation or improper use of Subordination Agreement;
 - (ii) Unauthorized use or disposition of funds or securities entrusted by a client to a Trading Participant in the course of its trading business including violation of securities borrowing and lending rules.
 - (iii) Trading-related Irregularities;
 - (iv) Failure to comply with a final and executory decision or order of CMIC, the CMIC Board or the Commission, in cases considered as grave or major violation;
 - (v) **Violation of Article VIII-A, Section 1 on RBCA ratio; and**

- (vi) Such other violations similar to the foregoing.
- (b) The following are considered **minor** violations:
- (i) Violation of capitalization requirements of a Trading Participant, subject to SEC Memorandum Circular No. 16 Series 2004 and the provision of Article VIII of this rules, **other than the violation of Article VIII-A, Section 1 of the latter;**
 - (ii) Violation of the Ethical Standards Rule;
 - (iii) Violation of the Code of Conduct and Professional Ethics for Traders and Salesmen;
 - (iv) Violation of **the Customer Protection Rule**, SRC Rule 49.2 on Customer Protection Reserves and Custody of Securities other than the violation set out in subparagraph (ii) of Section (3) (a) of this Article XII;
 - (v) Making untrue statements or the omission of any material fact required or necessary to be stated in CAIF, reports, records, books and documents submitted to CMIC for such not to be misleading; and
 - (vi) **All violations other than those mentioned in paragraph (a) Section 3 of Article XII.**

Section 4. *Types of Sanctions.* CMIC or the CMIC Board may impose the following disciplinary sanctions for violations of the Securities Laws by a Trading Participant in accordance with the following:

- (a) **Major** Violations
- (i) First violation – Written reprimand and fine in the amount of at least **Php50,000.00** but not exceeding **Php400,000.00**;
 - (ii) Second violation – **Fine of at least Php400,000.00 but not exceeding Php800,000.00 with a warning that a repetition of the same will merit the penalty of suspension;**
 - (iii) Third – **Permanent denial of (1) the exercise of the Trading Right and (2) access to the facilities and systems of the Exchange, (3) with a recommendation to the SEC for the revocation of the license of the Trading Participant.**
- (b) **Minor** Violations

- (i) First violation – Fine of at least **Php20,000.00** but not more than **Php60,000.00**;
- (ii) Second violation – Fine of at least **Php60,000.00** but not more than **Php100,000.00**;
- (iii) Third violation – Fine of at least **Php100,000.00** but not more than **Php150,000.00**;
- (iv) Fourth and subsequent violations – Fine of at least **Php150,000.00** but not more than **Php300,000.00**.

CMIC may order or impose such other remedies, which it deems proper and necessary, for a complete relief of the aggrieved party. Such remedies may include, but are not limited to, buy back of shares and furnishing of client documents.

Section 5. Mitigating and Aggravating Circumstances. In imposing the above disciplinary sanctions, CMIC or the CMIC Board may take into consideration the following mitigating and aggravating circumstances:

(a) Mitigating Circumstances – the penalty next lower than that prescribed for the rule violated may be imposed upon determination of the existence of the following:

- (i) First violation of Securities Laws including this Rules;**
- (ii) Amicable settlement by the parties;**
- (iii) No gross negligence or willful disregard of the rights of others attended the commission of the violation;**
- (iv) No significant risk or exposure to risk on the part of the client;**
- (v) Absence of malice or manipulative intent on the part of the offender; and**
- (vi) Correction or rectification of the offense within a reasonable period of time.**

(b) Aggravating Circumstances – the penalty next higher than that prescribed for the rule violated may be imposed upon determination of the existence of the following circumstances:

- (i) Repeated violations of Securities Laws and this Rules, which shall not be less than five (5), of rules of the same nature;**
- (ii) Gross negligence or willful disregard of the rights of others;**
- (iii) Significant risk or exposure to risk on the part of the client;**
- (iv) Malicious intent on the part of the offender to commit and/or conceal the violation;**
- (v) Failure to correct or rectify the offense within a reasonable period;**
- (vi) Considerable delay in the performance of the obligation; and**

(vii) Significant financial damage on the part of the client.

Section 6. Sanction on Registered Persons or Employees of the Trading Participant. CMIC or the CMIC Board may recommend to the Trading Participant and/or to the Commission the imposition of the following penalties on the Registered Person/s responsible for, or instrumental to the commission of, the violations of Securities Laws:

- (a) Suspension;**
- (b) Dismissal or expulsion; or**
- (c) Revocation of license.**

Section **7**. *Aggregation or "Batching" of Violations.* In imposing disciplinary sanctions, CMIC or the CMIC Board shall treat each count of violation as one and separate violation and shall not treat several counts of violations arising from the same set of facts as a single violation.

All previous violations within a six (6)-year period shall be taken into account in imposing sanctions for violations of similar nature.

Section **8**. *Publication of Disciplinary Action.* The CMIC shall inform the public of violations of these Rules or securities laws committed by and sanctions imposed, on Issuers and Trading Participants.

CMIC shall immediately publish at the Exchange or CMIC website the sanctions imposed on a Trading Participant as soon as (a) the CMIC Board affirms the sanctions, or (b) the period to appeal to CMIC Board lapses without the Trading Participant filing an appeal.

Section **9**. *Posting of Absence of Examination Findings.* CMIC shall post on the Exchange or CMIC website the list of Trading Participants whose regular and periodic audits by CMIC did not result in any Examination Findings.

Section **10**. *Payment of Fines.* An erring Trading Participant shall pay the penalty imposed by CMIC or the CMIC Board pursuant to an executory order or decision, within fifteen (15) calendar days from **the lapse of the period for filing the request for reconsideration to the CMIC Board and no such request is filed.**

In case a request for reconsideration filed within the prescribed period was denied by the CMIC Board, an erring Trading Participant shall pay the penalty imposed by the CMIC Board within fifteen (15) calendar days from receipt of the decision or resolution of the CMIC Board, regardless of any appeal which the erring Trading Participant may file from the decision of the CMIC or the CMIC Board.

If the erring Trading Participant fails to pay the penalty within the prescribed period and without need of any demand or order from CMIC or the CMIC Board, the erring Trading Participant shall additionally pay (a) a surcharge equal to twenty-five

percent (25%) of the imposed fine plus (b) interest of one percent (1%) for every day of delay based on the sum of the imposed fine and the surcharge.

If the erring Trading Participant fails to pay the fine and the surcharge and interests thereon within fifteen (15) calendar days from the lapse of the original fifteen-day period for the payment of the penalty, CMIC or the CMIC Board may suspend the erring Trading Participant.

Section 9. *Oversight Authority of the Commission.* The Commission shall have the authority to review the findings of the CMIC, re-classify the violations and impose the appropriate sanctions based on these rules and the applicable securities laws and regulations.

Sanction Guidelines Table

| <u>Major Violations</u> | Sanctions for <u>Major Violations</u> |
|--|--|
| <p>(i) Simulation or improper use of Subordination Agreement;</p> <p>(ii) Unauthorized use or disposition of funds or securities entrusted by a client to a Trading Participant in the course of its trading business including violation of securities borrowing and lending rules;</p> <p>(iii) Trading-related Irregularities;</p> <p>(iv) Failure to comply with a final and executory decision or order of CMIC, the MIB or the Commission, in cases considered as grave or major violation; and</p> <p>(v) <u>Violation of Article VIII-A, Section 1 on RBCA ratio;</u></p> <p>(vi) Such other violations similar to the foregoing.</p> | <p>(i) First violation - Written reprimand and fine in the amount of at least <u>Php50,000.00</u> but not exceeding <u>Php400,000.00;</u></p> <p>(ii) Second violation - <u>Fine of at least Php400,000.00 but not exceeding Php800,000.00 with a warning that a repetition of the same will merit the penalty of suspension;</u></p> <p>(iii) Third violation - <u>Permanent denial of (1) the exercise of the Trading Right and (2) access to the facilities and systems of the Exchange, (3) with a recommendation to the SEC for the revocation of the license of the Trading Participant.</u></p> |

Minor Violations

(i) Violation of capitalization requirements of a Trading Participant, **other than the violation of Article VIII-A, Section 1 of this rules;**

(ii) Violation of the Ethical Standards Rule;

(iii) Violation of the Code of Conduct and Professional Ethics for Traders and Salesmen;

(iv) Violation of SRC Rule 49.2 on **Customer Protection Rule**, Customer Protection Reserves and Custody of Securities other than the violation set out in subparagraph (ii) of Section (3) (a) of Article XII;

(v) Making untrue statements or the omission of any material fact required or necessary to be stated in CAIF, reports, records, books and documents submitted to CMIC for such not to be misleading; and

(vi) **All violations other than those mentioned in paragraph (a) Section 3 of Article XII.**

Sanctions for Minor Violations

(i) First violation – Fine of at least **Php20,000.00** but not more than **Php60,000.00;**

(ii) Second violation – Fine of at least **Php60,000.00** but not more than **Php100,000.00;**

(iii) Third violation – Fine of at least **Php100,000.00** but not more than **Php150,000.00;**

(iv) Fourth and subsequent violations – Fine of at least **Php150,000.00 but not more than Php300,000.00.**

ARTICLE XIII. MISCELLANEOUS POLICIES

Section 1. *Separability Clause.* These Rules shall be without prejudice to any applicable provisions of the Securities Laws. If any provision of these Rules shall be held to be contrary to any provision of the Securities Laws or any law, the remaining provisions shall continue to be in force and effect.

Section 2. *Effectivity.* These Rules shall be effective fifteen (15) days from its publication in the Exchange and CMIC website.