

RULES GOVERNING SECONDARY MARKET TRADE OF GOVERNMENT SECURITIES

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Pursuant to Section 129 of Republic Act No 7653, otherwise known as the New Central Bank Act, mandating the return of fiscal functions by the Bangko Sentral ng Pilipinas (BSP) to the Department of Finance (DoF), the following Rules are hereby promulgated to govern the secondary market trade of Government Securities:

Rule 1

Rationale for the Rules

- a. All dealings in securities are impressed with public interest, therefore, should be subject to prudential rules and licensing, such as, uniform calculation formulae and uniform accounting method and system
- b. Only Securities and Exchange Commission (SEC) licensed dealers can engage in the business of buying and selling securities.
- c. Members of the public can only buy from or sell to licensed dealers.
- d. Dealers must agree to certain conventions or practices to ensure an orderly, efficient, transparent and honest market of securities. These conventions should be articulated in writing and agreed to by prospective and licensed dealers.
- e. For this purpose, there must be adequate training and roster of eligible dealers, that is, trained and licensed. Such that, transfer of dealers from one institution to another should be subject to presentation of certificate of good conduct.

Rule 2

Objectives of the Rules

- a. The orderly registration and settlement of Government Securities (GS) trades in the secondary market.
- b. The convention of Delivery-Versus-Payment (DVP) and Real-Time-Gross-Settlement (RTGS) basis (transaction by transaction) of GS.
- c. The absence of systematic risk/disruption of the Philippine financial system.
- d. The efficiency, simplicity and transparency of the secondary market of GS.
- e. Lower cost of delivery/settlement of GS through electronic trading.
- f. Professionalization through ethical standards of trading.

Rule 3

Definition of Terms

For the purpose of these Rules, the following terms shall have the following meaning:

"Autodebit/Autocredit Authorization" shall mean an instruction in writing of dealers, in such form as hereby prescribed as being valid, to effect actual cash transfer between different Cash Accounts of a dealer or to the Cash Account of another dealer;

"Bureau" shall refer to the Bureau of Treasury or its officials, in appropriate cases;

"Book-entry delivery" shall mean a method of delivering securities which is constructive, not physical, that permits trades to settle by debiting or crediting securities accounts by book entry;

"Commission" shall refer to the Securities and Exchange Commission or its officials, in appropriate cases;

"Dealer" shall mean any person as defined in Section 2 of the Revised Securities Act or its amendments;

"Delivery-Versus-Payment" or "DVP" shall mean a method of executing transaction in which the buyer receives trade securities from the seller only against buyer's full payment for the securities; conversely, the seller delivers trade securities to the buyer only against receipt of buyer's full payment;

"Pledge Instruction" shall mean an instruction of a Dealer, in such form as hereby prescribed as being valid, to earmark Government Securities in his Securities Account in favor of another Dealer or the Settlement Bank or any pledgee;

"Real-Time-Gross-Settlement" or "RTGS" shall mean an immediate settlement of the transactions in GS through electronic processing without any netting;

"Securities Account" shall mean each account and sub-accounts allocated to and administered by dealers in which GS owned by or pledged to or lent to of such dealers are credited; conversely, or from which GS sold by or pledged by or borrowed by such dealers are debited;

"Settlement Account" shall mean, in relation to each dealer, the cash account maintained with the Settlement Bank for the purpose of paying for GS transaction;

"Settlement Bank" shall mean the bank designated and approved by the Bureau for the money payment purposes of GS transactions;

"Trade Instruction" or "TI" shall mean an instruction of a dealer, in such form as hereby prescribed as being valid, to effect book-entry delivery of GS to a Securities Account or Securities Sub-Account of a dealer, or to the Securities Account or Securities Sub-Account of another dealer.

Rule 4

Persons to Trade

Only dealers who wish to engage in the regular business of buying and selling GS after accessing the Registration of Scripless Securities (RoSS) may trade in GS.

Such dealer shall meet the following:

- a. Currently licensed by the Commission to deal in securities; and
- b. Undertaking to comply with any law, regulation, order or convention and any requirement pursuant thereto, applicable to persons who deal in GS; and
- c. Execution of Autocharge, Autocredit and Autopledge to/from a Cash/Securities Account to/from another.

Rule 5

Person Not Authorized to Trade

Non-dealer may access the System through a dealer with whom proper bilateral funding arrangements shall have been concluded.

Rule 6

Procedures for Trading

Trading shall be done through an electronic dealing system, in the following manner:

6.1 Outright Sale/Purchase

- Dealers shall input the corresponding trade instruction (Confirmation of Outright Sale of GS for the selling dealer and Confirmation of Outright Purchase of GS for the purchasing dealer), which will be matched by the Bureau with the Settlement Bank and when matched, the relevant transaction shall be cleared by the Bureau.
- Based on the trade instruction of the dealers, the Bureau shall verify the sufficiency of GS in the Securities Account of the selling dealer and the sufficiency of cash in the Settlement Account of the paying dealer. Once matched, the Bureau shall clear the transaction by causing the relevant amount to be debited and credited on the respective Settlement Account of the dealers. Simultaneously, the Bureau shall debit the Securities Account of the selling dealer and credit the Securities Account of the purchasing dealer.

6.2 Repurchase/Resell Agreement

- Dealers shall input the corresponding trade instruction (Confirmation of Sale of GS with an Obligation to Repurchase for the selling dealer and Confirmation of Purchase of GS with an Obligation to Resell for the purchasing dealer), and based on the same, the Bureau shall verify the sufficiency of GS in the Securities Account of the selling dealer and the sufficiency of cash in the Settlement Account of the paying dealer.
- Once the securities in the Securities Account of the selling dealer and the cash in the Settlement Account of the paying dealer matched, the Bureau shall clear the transaction by causing the simultaneous debit and credit of the relevant amount on the respective Settlement Account of the dealers and the debit and credit of the relevant GS on the respective Securities Account of the dealers.
- Failure of a dealer to repurchase/resell GS subject of his Repurchase/Resell Agreement within the stipulated period shall subject such dealer to a penalty for every day of delay in repurchasing/reselling relevant GS in accordance with the Revised Securities Act.

6.3 Lending/Borrowing

Lender-dealer shall input a Confirmation of GS Lending in favor of the Borrower-dealer, who, in turn, shall input a Confirmation of GS Borrowing. Based on the same, the Bureau shall verify the availability of free GS in the Securities Account of the Lender-dealer. Once verified, the Bureau shall clear the transaction by causing the relevant GS to be debited and credited on the respective Securities Account of the Lender-dealer and Borrower-dealer.

6.4 Pledge

- Pledgor-dealer shall input a Pledge Instruction and based on the same, the Bureau shall verify the availability of free GS in the Securities Account of the Pledgor-dealer. Once verified, the Bureau shall clear the transaction by causing the relevant GS to be earmarked in favor of the Pledgee.
- Pledged GS shall not be eligible for any trade transaction unless the Pledgor-dealer and Pledgee input the

necessary instruction for the release of the same.

Rule 7

Procedures for Settlement

7.1 DVP and RTGS

Settlement of all GS transactions will always be on a Delivery-Versus-Payment (DVP) basis, i.e., delivery will be simultaneous with payment, and on a Real-Time-Gross Settlement (RTGS) basis, i.e., trade for trade and not netting.

7.2 Securities Account and Settlement Account

Each dealer shall maintain a Securities Account with the Bureau and a Settlement Account with the Settlement Bank.

7.3 Autodebit/Autocredit Authorization

Each dealer shall authorize the Bureau in writing, through an autocharge/autocredit authorization, to debit/credit their Securities Account upon debit/credit instruction, and the same autocharge/autocredit for the Settlement Bank to debit and/or credit their Settlement Account.

7.4 Money Position and Estimated Trade

At the start of trading hours, each dealer should know and validate the funds available in his Settlement Account. Further, each dealer shall calculate the amount needed for his trade settlement for the day.

7.5 Overnight Lending

If the Settlement Account balance of a dealer in his estimation is not sufficient for his estimated deals for the day or in any event of insufficiency of funds of a dealer, such dealer should make an arrangement with the Settlement Bank for an Overnight Lending collateralized by free GS in the dealer's Securities Account with the Bureau, subject to the terms and conditions of the Settlement Bank.

It shall be the duty of the Settlement Bank to inform the Bureau of its Overnight Lending to dealers and to re-request earmarking lending to dealers and to request earmarking of subject GS in its favor.

7.6 Documentary Stamp Tax Payments

It shall be the obligation of dealers to ensure that all Documentary Stamp Tax (DST) due on their GS transactions are paid,

Rule 8

Accounting Requirements

8.1 Duty to keep records

It shall be the responsibility of each dealer to keep and maintain at all times a proper system of books and records necessary to record properly its business transactions and financial charts in accordance with the prescribed accounting system, including, without limitation:

a. blotters (or other records of original entry) containing an itemized daily record of all purchases and sales of securities, all receipts and deliveries of securities, all receipts and disbursements of cash and all other debits and credits. Such record shall show the account for which each transaction was effected, the trade dates and

description of the securities;

b. a general ledger (or other records) maintained in detail reflecting all assets and liabilities, income and expense and capital accounts; and

c. ledger accounts (or other records) itemizing separately as to each cash and securities account of every client, all purchases, sales, securities and all other debits and credits to such account.

8.2 Accounting System for GS

8 2.1 Treasury Bills

a. Purchase of Treasury Bills

Dr. Investments in T/Bills xxx

Dr. Prepaid Final Tax xxx

Cr. MC/Cash/Due from BSP xxx

b. Amortization of T/Bills at the end of month

i. Interest Income = (Discount)(Days run/Original Term)

Dr. Investments in T/Bills xxx

Cr. Interest Income xxx

ii. Income Tax Incurred = (W/holding Tax) (Days run/Original Term)

Dr. Provision for Income Tax xxx

Cr. Prepaid Final Tax xxx

c. Sale of Treasury Bills

Dr. MC/Cash/Due from BSP xxx

Cr. Prepaid Final Tax xxx

Cr. Trading Gain/(Loss) xxx

Cr. Investments in T/Bills xxx

d. Closing of Prepaid Final Tax

Dr. Trading GainZ(Loss) xxx

Cr. Prepaid FinalTax xxx

FORMULA FOR PRICING T-BILLS

a. Purchase Price (PP) (Pre-Tax) = $FV (360)/360 + (Y) (T)$

Discount = $FV - PP (Pre-Tax)$

W/holding Tax = $Discount \times Tax Rate$

PP (after Tax) = $PP (Pre-Tax) + W/ holding Tax$

b. Selling Price (SP) (Pre-Tax) = $FV (360)/360 + (Y) (\# \text{ of days to run})$

Discount = $FV - SP (Pre-Tax)$

W/holding Tax = Discount x Tax Rate

SP (after Tax) = SP (Pre-Tax) + W/holding Tax

c. Interest Income earned - PP (Pre-Tax) (Y)
(orig. term - # of days to run /360)

d. Trading Gain/(Loss) = SP (Pre-Tax) - PP
(Pre-Tax) - Interest Income Earned

8.2 2 Treasury Bonds FORMULA FOR PRICING T-BONDS

a. When simply carried in GSEDs' books.

Month-end accruals are booked as follows:

Face Value x coupon rate x, days-run/360

Dr. Accrued Interest Receivable xxx

Cr. Interest Income (net of tax) xxx

Cr. Taxes Payable xxx

Current Yield Computations, coupon/price (as determined by market) Yield to Maturity (conventional method)

b. When T-Bonds are sold in the Secondary Market (Price Quoted)

If sold at premium, i.e. 101

Principal is (FV x 1.01) xxx

Accrued interest (FV x CR x TE) xxx

Taxes Payable (xxx)

Net Sale Price xxx

Dr. MC/Cash xxx

Dr. Taxes Payable xxx

Cr. Trading Accounts Sec./Inv. xxx

Cr. Trading Gains xxx

Cr. Accrued Interest Receivable xxx

Yield Equivalent Calculations

Current Market Yield xxx

Yield to Maturity xxx

Return (CD-ACT/360) xxx

8.3 Duty to check accuracy of statement of accounts and reports

It shall be the responsibility of each dealer to check and reconcile with its own records the statement of accounts and reports generated by the System in relation to the clearing and settlement of GS and to properly notify the Bureau in writing of any error or omission contained therein.

Rule 9

Operating Forms

In connection with the RoSS, the following forms are to be used by the dealers:

- a. Confirmation of Outright Sale/Purchase (see Appendix "A"[*]): a document to be prepared in triplicate by Seller/Purchaser-dealer and signed by its authorized signatory, confirming to the Bureau that it has sold/purchased unto/from Buyer/Seller-dealer the GS described thereat;
- b. Confirmation of Sale/Purchase of GS with an Obligation to Repurchase/Resell (see Appendix "B"[*]): a document to be prepared in triplicate by Seller/Purchaser-dealer and signed by its authorized signatory, confirming to the Bureau that it has sold/purchased unto/from Buyer/Seller-dealer with an obligation to repurchase/resell the GS described thereat;
- c. Confirmation of GS Lending/Borrowing (see Appendix "C"[*]): a document to be prepared in triplicate by Lender/Borrower-dealer and signed by its authorized signatory, confirming to the Bureau that it has lent/borrowed unto/from Borrower/Lender-dealer the GS described thereat; and
- d. Declaration of GS Pledge Transaction (see Appendix "D"[*]): a document to be prepared by the Pledgor-dealer and signed by its authorized signatory, declaring that is has entered into a pledge transaction pledging the GS described thereat.

Rule 10

Records Examination

All accounts, forms, books and other records of dealers shall be subject to such reasonable periodic examination by the Commission as the Commission may deem necessary and/or appropriate in the interest of the public and/or for the protection of GS investors.

Rule 11

Market Ethics

11.1 General

In the trading of GS, all dealers must:

- a. Observe high standards of ethics and conduct in the transaction of their business;
- b. Not engage in any business conduct or practice which is unbecoming or detrimental to the public interest; and
- c. Be of such character and business repute and have such experience and training as is consistent with the standards described in clauses (a) and (b).

11.2 Acts Subject to Disciplinary Actions

The Bureau may institute disciplinary proceedings against a dealer in respect of an act of misconduct committed by it. Such act of misconduct includes:

- a. a breach of these Rules;
- b. a failure to comply with any condition or requirement for the RoSS;
- c. being subject to an adverse finding by any competent authority such as any court of competent jurisdiction, the Commission or any other organization to which the dealer is subject;
- d. errors, delays or other conduct detrimental to the operations of the RoSS or conduct which is detrimental to the interest of other dealers or the public, in general;

- e. selling without inventory or expectation of inventory of securities or buying securities without funds or credit line available;
- f. participating or knowingly allowing its name to be used in respect of any advertisement or sales literature in connection with GS which is false, misleading, or inaccurate in material particular;
- g. engaging in GS unauthorized transactions;
- h. engaging in "churning" or excessive trading; and
- i. failure to pay a fine or comply with any other disciplinary action imposed against a dealer.

11.3 Disciplinary Actions

11.3.1 Without prejudice to any other right the Bureau may have, on each charge admitted by or proved against a dealer, the Commission may take no action or impose any one or more of the penalties below:

- a. expel the dealer from the RoSS;
- b. suspend the dealer from the RoSS,
- c. impose a fine on the dealer;
- d. publicly censure the dealer; and
- e. take such other disciplinary action/s as the Bureau shall consider appropriate in the circumstances.

11.3.2 The imposition of the any of the foregoing disciplinary action shall be without prejudice to the filing of any charge against violator-dealer.

11.4 Procedures for the Imposition of a Disciplinary Action

The following procedures shall apply where the Commission proposes to take disciplinary action against a dealer:

- a. the Commission shall inform such dealer in writing the situation which gives rise to the Commission proposing to take disciplinary action against it together with a concise statement of the facts;
- b. the dealer in question shall have the right within a period of fifteen (15) days after notification to serve a written statement upon the Commission for the purposes of explaining fully the conduct complained of and to serve a written notice calling for a meeting;
- c. if a dealer calls for a meeting, the same should be held on a date and at a time and place determined by the Commission, who shall give notice to the dealer of the date, time and place of such meeting not less than five (5) days before the same is due to be held. The dealer shall have the right to attend such meeting and to make representations as to whether proposed disciplinary action should or should not be taken; and
- d. the Commission shall immediately notify the GSED in writing of its decision with regard to the taking of disciplinary action.

11.5 Appeal

GSEDs may appeal the decision or order of the Commission in accordance with Presidential Decree No. 902-A, as amended.

Rule 12

Effectivity

These Rules shall take effect immediately and shall be published once in at least one newspaper of general circulation or in the Official Gazette.

Adopted: 17 Oct. 1996

(SGD.)PERFECTO R. YASAY, JR.
Chairman

(SGD.) FE ELOISA C. GLORIA
Associate Commissioner

(SGD.) EDIJER A. MARTINEZ
Associate Commissioner

(SGD.) DANILO L. CONCEPCION
Associate Commissioner

[*] Text Available at Office of the National Administrative Register, U.P. Law Complex, Diliman, Q.C.

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