NATIONAL ADMINISTRATIVE REGISTER · [ BSP MEMORANDUM, MAY 11, 2005 ] · JANUARY 28, 2004

# PROCEDURES TO BE OBSERVED IN INVESTING IN CREDIT-LINKED NOTES, STRUCTURED PRODUCTS AND SECURITIES OVERLYING SECURITIZATION STRUCTURES

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In line with the policy of encouraging banks to diversify their investment portfolios and to foster the development of a market for new financial products, the BSP has issued guidelines on the investment of Universal Banks (UBs) and Commercial Banks (KBs) in (1) credit-linked notes and similar products (Circular No. 417 dated 28 January 2004), (2) foreign currency denominated structured products (Circular Nos. 466 and 469 dated 05 and 13 January 2005, respectively) and (3) securities overlying securitization structures (Circular No. 468 dated 12 January 2005).

No prior BSP approval is required to enter into authorized transactions. However, it shall be the responsibility of UBs/KBs to fully comply with appropriate risk management standards including, as a minimum, those prescribed under relevant Circulars. The following regulatory requirements shall be fully complied with UBs/KBs investing in products allowed under Circulars Nos. 417, 466/469 and 468:

1. Submit the following documents to the appropriate supervision and examination department of the BSP within five (5) banking days after the date of its initial investment in credit-linked notes, structured products and/or securities overlying securitization structures --

a. A notarized certification in the attached format (refer to Annexes "A" and "B") duly signed by the President/Chief Executive Officer or its equivalent, the Treasurer and Compliance Officer, stating that the bank's investments are in compliance with relevant BSP rules and regulations, and that the bank has an adequate risk management system in place; and

b. Terms and conditions and/or product manuals on the credit-linked notes, structured products and/or securities, overlying securitization structures, which as a minimum should cover the following:

i. Description of relevant financial product;

ii. Analysis of the proposed investments'-

1) reasonableness vis-a-vis the institution's overall financial condition and capital levels; and

2) consistency with the institution's business strategies and objectives;

iii. Analysis of the risks that may arise from the investments and the corresponding impact on the bank's risk profile;

iv. Procedures/methodologies that the bank will implement to measure, monitor and control the risks inherent in the financial products;

v. Relevant accounting guidelines, including pro-forma accounting entries;

vi. Relevant tax treatment;



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vii. Analysis of any legal/regulatory restrictions and whether the investment is permissible for the institution; and

viii. Process flow chart, from deal initiation to risk reporting, indicating the departments and personnel involved in the identified processes.

UBs/KBs failing to submit the required certification within the prescribed deadline shall be subject to monetary penalties applicable for delayed reporting under existing regulations. For purposes of imposing monetary penalties, the required certification shall be classified as a Category A-1 report. Further, failure to comply with the above requirements shall subject the erring bank to the imposition of administrative sanctions under Section 37 of R.A. 7653 (The New Central Bank Act).

The certification and the terms and conditions and/or product manual need not be submitted for a bank's subsequent investments in the same issue of credit-linked note or structured product, or securities overlying the same tranche of a securitization structure.

2. The certification shall be subject to post-verification by the appropriate supervision and examination department of the BSP.

Should the BSP subsequently determine that the investments do not fully comply with the provisions of BSP Circular Nos. 417, 466/469 and 468, as applicable, and other relevant BSP regulations, the UB/KB shall be considered to have submitted a false certification, subject to the sanctions prescribed under --

a. BSP Circular No. 466 for investments in structured products by UBs and KBs without expanded derivatives authority, or

b. Section 37 of R.A. No. 7653 for investments in structured products by UBs and KBs with expanded derivatives authority, and for investments in credit-linked notes and similar products and in securities overlying securitization structures by all UBs and KBs.

Monetary penalties shall be reckoned from the date of the investment until the date that the erring bank shall have fully complied with the requirements under Circular Nos. 417, 466/469 and 468 and other relevant BSP regulations.

For information and guidance.

Adopted: 11 May 2005

(SGD.) NESTOR A. ESPENILLA, JR.
Deputy Governor


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