



OFFICE OF THE GOVERNOR

CIRCULAR NO. 466
Series of 2005

The Monetary Board, in its Resolution No. 1791 dated 09 December 2004, approved the following guidelines allowing universal and commercial banks without expanded derivatives authority to invest in certain specified structured products without need of prior Monetary Board approval:

1. **Statement of Policy**

The Bangko Sentral ng Pilipinas (BSP) encourages banks to diversify their expanded foreign currency deposit unit (EFCDU) investment portfolios in order to stabilize earnings, control maturity mismatches and minimize overconcentration of exposures.

2. **Scope**

EFCDUs of universal banks (UBs) and commercial banks (KBs) without expanded derivatives authority may invest, for their own account, in foreign currency-denominated structured products issued by banks and special purpose vehicles (SPVs) of high credit quality; Provided, that the revenue streams of such products may only be linked to interest rate indices and/or foreign exchange rates other than those that involve the Philippine Peso; Provided, further, that the minimum all-in return of such investments may not be lower than zero. For purposes of this Circular, structured products do not include asset-backed securities, credit-linked notes and other similar instruments.

3. **Other Conditions**

- a. **Maturity** – The maximum contractual maturity of any investment in structured products shall be 5 years.
- b. **Credit quality of issuer** – Acceptable issuers are banks and SPVs collateralized by securities rated at least "A" or its equivalent by an international rating agency acceptable to the Monetary Board.
- c. **Booking** – Investments in structured products as herein defined shall be booked under the account *Investments in Bonds and Other*

PANANALAPING MATATAG, BANSANG PANATAG

Debt Instruments (IBODI), except for instruments with put options which shall be booked under the *Available for Sale Securities (ASS)* account.

d. **Prudential limits** – The total carrying value of all investments in structured products as defined herein at any given point in time must not exceed 20% of the total investment portfolio of the EFCDU (combined amount of Trading Account Securities (TAS), ASS and IBODI).

e. **Risk Management** – Investing banks must have established internal processes to identify, evaluate, monitor and manage the risk exposures, e.g. credit risk, market risk, liquidity risk, operational risk, legal risk, compliance risk, created by their investments in structured products. As a minimum:

- i. Such investments must be specifically approved by the Board of Directors and be subject to appropriate internal limits and periodic reporting to the Board.
- ii. Banks must comply with generally accepted accounting and disclosure standards and/or rules and regulations prescribed by the BSP.
- iii. An independent risk management function must be in place.
- iv. Banks should have the ability to value their investments on a continuing and consistent basis and to measure their sensitivity to market movements. This should include performing, at regular intervals, stress tests that reflect extreme market conditions. As part of the valuation exercise, banks should be able to obtain bid prices from the issuers of the investment instruments on a monthly basis.
- v. Management should ensure that the risks of the investments are accurately aggregated in risk reports on a timely basis.

4. Capital Treatment

The capital treatment shall be in accordance with existing rules and regulations as modified for structured instruments.

5. Eligibility as EFCDU Asset Cover

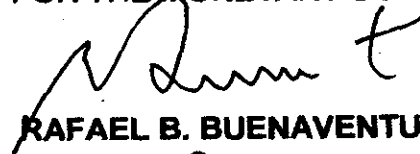
Investments in structured notes shall qualify as asset cover, but not as part of the 30% liquidity cover for EFCDU liabilities.

6. Sanctions

Non-compliance with the provisions of this Circular shall subject the bank to a fine of one-tenth of one per cent of the outstanding investment per day, but not to exceed P30,000 per day, to be reckoned from the day the bank is deemed in violation of regulations, until the day the bank has complied with the requirements. Banks may also be temporarily or permanently prohibited from such investments as circumstances may warrant.

This Circular shall take effect fifteen (15) days following its publication either in the Official Gazette or in a newspaper of general circulation.

FOR THE MONETARY BOARD:



RAFAEL B. BUENAVENTURA
Governor

5 January 2005