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SECURITIES AND EXCHANGE COMMISSION
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Market Regulation Department

SEC-MRD Opinion No. 3
Series of 2008

December 18, 2008

DEUTSCHE BANK AG
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Ayala Triangle, Makati City
Fax: 894-6901

*Attention: Atty. Rhonell S. Fajardo, Country Chief Operating Officer
Ms. Marla Corazon Ordenez, Investment Banking Operations*

Subject: Delivery versus Payment (DVP)

Gentlemen:

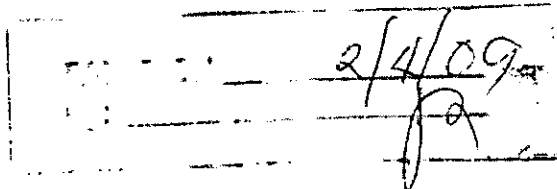
This refers to your request for opinion on the issue whether or not the settlement procedures of your bank with qualified institutional buyers (QIBs) with regard to your government securities (GS) transactions outside of the eDVP system of PDEX achieve delivery versus payment, and hence compliant with SEC Memorandum Circular No. 14, series of 2006, otherwise known as the Rules Governing the Over-the-Counter (OTC) Market.

In particular, you cited Section 20 (B) of the OTC Rules which requires that "the clearing and settlement arrangement in the exchange of assets subject of the trade shall be delivery versus payment (DVP) scheme".

In reply, herein below is our response to your query:

This is not the first time our office is addressing this issue. In *SEC-MRD Opinion No.1 dated 28 July 2008*, we described the different approaches of achieving DVP in securities transactions. We also discussed extensively the different settlement systems in the domestic equities and fixed income markets. We also made a ruling on similar issue in *SEC-MRD Opinion No.2 dated 8 October 2008*.

The process of clearing and settling securities trade includes several key steps. *First*, the confirmation of the terms of trade by the market participants. *Second*, the calculation of the obligations of the counterparties resulting from the confirmation process



*received
on 2/5/09*

which is known as clearance. *Third*, the final transfer of securities (delivery) in exchange for the final transfer of funds (payment) in order to settle the obligations which is known as settlement.

A DVP system is a securities settlement system that provides a mechanism that ensures that delivery occurs if and only if payment occurs. It is a procedure by which the buyer's payment for securities is due at the time of delivery. The purpose of DVP system is to ensure that counterparties are not exposed to principal risk, that is, the risk that the seller of a security could deliver but not receive payment or that the buyer of a security could make payment but not receive delivery. *[CPSS, Delivery Versus Payment in Securities Settlement Systems (BIS, September 1992)]*

Strictly speaking, DVP does not require simultaneous final transfers of funds and securities. When a central securities depository does not itself provide cash accounts for settlement, it first blocks the underlying securities in the account of the seller or his custodian. It then requests transfer of funds from the buyer to the seller in the settlement bank. The securities are delivered to the buyer or his custodian if and only if the central securities depository receives confirmation of settlement of the cash leg from the settlement bank. *[CPSS, Recommendations For Securities Settlement Systems (BIS, November 2001)]*

In your request, you seek confirmation that the settlement procedures by Deutsche Bank Manila (DBMN) relative to your GS transactions with QIB clients achieve DVP. Based on your letter and Manual of Procedures, your bank's settlement procedures can be described in general as follows:

TRADE CAPTURE AND CONFIRMATION. Once a deal is entered by a DBMN salesperson, the following are generated: trade ticket and trade confirmation. The trade ticket and trade confirmation contain the counterparty's name, sell/buy trade, trade date, settlement date, international securities identification number, nominal amount and settlement amount. Then, the back-office personnel will conduct a phone confirmation to match all the details of the transaction per trade ticket, while the trade confirmation is sent via auto-fax to the counterparty on trade date. Counterparty may also refer to counterparty's designated custodian.

CLEARING AND SETTLEMENT. In **BUY Trades** (where DBMN buys securities from counterparty), the following process is observed:

1. Counterparty delivers instruction to DBMN containing details where the security will come from and where the funds should be remitted.

2. Counterparty enters a Sell Value Received trade in Registry of Scripless Securities (RoSS) Telerate system facing DBMN.

3. DBMN credits the Accounts Receivable/ Accounts Payable (ARAP)-Unsettled Deal Account in the amount of the payment due to the counterparty to earmark said amount in its favor.

The ARAP-Unsettled Fixed Income/Debt Securities (FI/DS) Deal Account is used to temporarily lodge the counterparty's payment made via the Philippine Payments and Settlement Systems (PhilPass), as well as DBMN's payment to counterparty (whether via PhilPass or credit to counterparty's account), to earmark said funds. PhilPass is the real

time gross settlement system for peso payments operated by Bangko Sentral ng Pilipinas (BSP).

Once the security has been delivered and posted to the counterparty's account (in case of a DBMN sell deal) or to DBMN's account (in case of a DBMN buy deal), the funds will be released in favor of the seller. This account will be closely monitored by FI/DS Operations unit and shall always have zero "0" balance at end of day.

4.DBMN inputs the payment instruction into the relevant cash settlement system, depending on counterparty's instruction either via MT103 in PhilPass or via credit to counterparty's deposit account with DBMN in IDMS. MT103 is swift message type 103 for corporate or non-bank counterparty used for single customer credit transfer. IDMS or integrated data management system is a back end settlement system used for customer set up, transaction processing, settlement and accounting entry generation. It is also used as a sub-ledger for all postings related to clients' cash account settlement.

5.DBMN accepts the sell notification of counterparty also via RoSS Telerate.

In case of RoSS Telerate system failure or where counterparty does not have Ross Telerate, the following manual settlement procedures are observed: (a) DBMN prepares and faxes confirmation of purchase (COP) to counterparty and sends the original to the counterparty; (b) Counterparty prepares a confirmation of sale (COS) and faxes both the COS and COP to the Bureau of Treasury (BTR). Counterparty will send the original COS & COP to the BTR.

6.DBMN checks if the security has been successfully delivered to DBMN's securities account by confirming if the status is "posted" in RoSS Telerate system or, in the case of manual settlement, by calling the BTR before 1:00 P.M.

7.Once confirmation of security delivery is done, DBMN will release the earmarked fund and authorize the credit to counterparty's account in IDMS, if payment is via credit to said account, or the remittance to the BSP account of counterparty's bank, if payment is via PhilPass. If DBMN pays via MT103 in PhilPass, DBMN will then receive an MT012f sender's notification message from the BSP to indicate that the BSP has carried out instructions to pay counterparty. MT012f is swift message type sender notification usually received from BSP notifying that DBMN debit instruction had been effected.

8.If the security has not been delivered, DBMN shall reverse its payment instruction.

In **SELL Trades** (where DBMN sells securities to counterparty), the following process is observed:

1.Counterparty delivers instruction to DBMN containing details on the settlement of securities, including payment details. In case of RoSS Telerate system failure or where counterparty does not have RoSS Telerate, counterparty prepares and faxes a COP to DBMN and sends the original COP to DBMN.

2.1 If counterparty pays DBMN via PhilPass (by posting to DBMN's account with BSP), DBMN has to check incoming MT103 or MT202 in MINT and debit the ARAP-Unsettled FI/DS Deal Account with the amount of the funds received to earmark payment

to DBMN. MT202 is the swift message type for general financial institution transfers. MINT is platform which provides messaging layer for financial messages Swift, Fax and Telex formats.

2.2 If counterparty pays DBMN via PhilPass via authority to debit counterparty's account with DBMN in IDMS, DBMN has to block/earmark client's account in IDMS.

3.DBMN proceeds to input the Sell Value Received trade in RoSS Telerate System facing the counterparty. Counterparty accepts the sell notification sent by DBMN also in RoSS Telerate.

In case of Ross Telerate system failure or where counterparty does not have RoSS Telerate, DBMN prepares as COS and faxes both the COS and COP to BTR. DBMN will send the original COS & COP to the BTR.

4.DBMN checks if the security has been successfully delivered to counterparty's securities account by confirming if the status is "posted" in the RoSS Telerate system or, in the case of manual settlement, by calling the BTR before 1:00 P.M.

5.Once confirmation of security delivery is done, DBMN will release the earmarked funds and authorize the debit from counterparty's account in IDMS if payment is via debit to said account, or reverse the ARAP-Unsettled FI/DS Deal Account if payment is via remittance in PhilPass.

6.If the security has not been delivered, DBMN shall not debit client's account and shall return funds received via PhilPass.

The following cut-off times are observed:

Receipt/Delivery of securities in RoSS Telerate --- 1:30 P.M.

Receipt/Payment of cash -----1:30 P.M.

Under the above transactions, whether buy or sell, settlement will be done on a per deal basis and will not involve netting or off-setting of transactions.

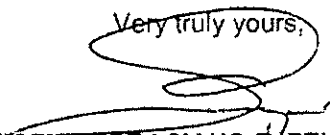
These procedures and safeguards ensure that each transfer of securities is effected only when payment occurs or assured within the settlement cycle. As earlier mentioned, DVP does not require simultaneous final transfers of funds and securities. It is essential though that the securities are delivered to the buyer or his custodian if and only if it is confirmed that the cash aspect of the transaction is paid. Thus, in our view, the **settlement arrangements described in your letter and Manual of Procedures achieve DVP.**

It is understood though that the foregoing opinion is rendered based solely on the facts you disclosed and described in the query and relevant solely to the particular issue raised therein and shall not be used in the nature of a standing rule binding upon the Commission in other cases whether of similar or dissimilar circumstances. *[SEC Memorandum Circular No. 15 (2003)]*

Finally, you are directed that DBMN's Manual of Procedures for GS transactions with QIBs be made part of your records and that the same shall be disclosed to your counterparties and form part of the client agreement.

Thank you.

Very truly yours,


VICENTE GRACIANO P. FELIZMENIO JR.
Officer in Charge

Paid: OR # 0207178
Filing Fee: P5,000.00