Securities and Exchange Commission
PHILIPPINES

SEC Memorandum Circular No. 21
Series of 2019

TO : **ALL INVESTMENT COMPANIES**
FUND MANAGERS
OTHER ENTITIES DEALING WITH INVESTMENT COMPANIES

SUBJECT : **RULES ON THE APPOINTMENT OF INDEPENDENT OVERSIGHT ENTITY, INDEPENDENT NET ASSET VALUE CALCULATION, QUALIFICATIONS OF KEY OFFICERS OF FUND MANAGERS, AND LIQUIDATION OF ASSETS AND WINDING UP OF INVESTMENT COMPANIES**

Section 35(a) of Republic Act No. 2629, or the Investment Company Act (ICA), and Section 72 of Republic Act No. 8799, or the Securities Regulation Code (SRC), vest upon the Securities and Exchange Commission the authority to make, issue, amend, and rescind rules and regulations and orders which are necessary or appropriate to the exercise of the powers conferred upon it in the ICA and the SRC. For purposes of its rules and regulations, the Commission may classify persons, securities and other matters within its jurisdiction and prescribe different requirements for different classes of persons, securities or matters.

To enhance the regulatory compliance of Investment Companies and their Fund Managers, and to ensure adequate protection for shareholders and unitholders, the following rules are hereby adopted:

I. Independent Oversight Entity (IOE)

An Investment Company shall perform oversight over its Fund Manager. Hence, the former is required to have an Independent Oversight Entity which shall function as an impartial committee or entity tasked to monitor the transactions and functions carried out by the Fund Manager.

A. Definition of Terms

a. Executive Director – a director who is also the head of a department or unit of the Investment Company or performs any work related to its operation
b. Non-executive director – a director who is not the head of a department or unit of the Investment Company nor performs any work related to its operation
c. Independent Director – a person who, apart from his fees and shareholdings, is independent of management and free from any business or other relationship which could, or could reasonably be perceived to, materially interfere with his exercise of independent judgment in carrying out his/her responsibilities as a director
d. Independent Oversight Entity (IOE) - an impartial committee or entity tasked to monitor the transactions and functions carried out by the Fund Manager
e. Affiliate – refers to an entity that holds directly/indirectly at least 10% or more of the total number of issued shares in the Investment Company, Fund Manager, or vice versa, or have a common shareholder that holds directly/indirectly 10% or more of the total number of the issued share capital of the Investment Company or Fund Manager

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B. Constitution or Engagement of an IOE

An Investment Company may constitute its Audit Committee as its IOE or may engage the services of a custodian bank, trust entity or an external auditor to serve as such.

1. Audit Committee of the Investment Company as IOE

To qualify as an IOE, the Audit Committee must be composed of at least three (3) non-executive directors, the majority of whom, including the Chairperson, should be independent. In order to ensure independence and prevent conflict of interest, the members of the Audit Committee shall not be allowed to hold interlocking directorships in other entities involved in the operation of the Investment Company such as the Fund Manager, Fund Distributor, Fund Advisor, Transfer Agent and Custodian.

The members of the Audit Committee must have relevant background knowledge, skills and experience in the areas of accounting, auditing, finance, capital markets and/or other related fields.

Upon the election of directors, the board shall promptly constitute its Audit Committee. The names of the members of the committee shall be reported to the Commission, through a Current Report (SEC Form 17-C), and reflected in the General Information Sheet (GIS), along with the results of the elections.

A maximum cumulative term limit of nine (9) years shall be observed by independent directors serving as members of the Audit Committee pursuant to SEC Memorandum Circular No. 4, Series of 2017. No member of the Audit Committee may be removed as such by reason of his/her performance of duties under this Circular.

The constitution of the Audit Committee, as well as its functions and responsibilities, shall be reflected in the Investment Company's Manual of Corporate Governance.

2. Custodian Bank, Trust Entity or External Auditor as IOE

The Investment Company may appoint a custodian bank, trust entity or an external auditor as its IOE, subject to the same limitations under item II(A) (1-2) of this Circular, that it is not affiliated with the Fund Manager and Investment Company.

C. Roles and Responsibilities of an IOE

The IOE shall:

1. Exercise care and diligence when monitoring the transactions and functions of the Fund Manager;
2. Oversee the transactions and functions of the Fund Manager to ensure compliance with the disclosures made in the Registration Statement (RS), prospectus, the Investment Company Act, Securities Regulation Code and their implementing rules and regulations (IRR). For cross-border offerings or transactions, in addition to the abovementioned, oversee the transactions of the Fund Manager in order to ensure that it also complies with the standards/requirements of bilateral or multilateral agreements allowing cross-border offering/transaction that the Philippines is party to;
3. Oversee the subscription and redemption of shares or units facilitated by the Fund Manager and to approve the request of the Fund Manager in the case of suspension of redemption of shares or units whenever necessary for the protection of the investors subject to the rules on Suspension of Redemption provided under Rule 10.4 of ICA-IRR;

4. Oversee the activities of the Fund Manager in order to ensure that it complies with the rules on investment restrictions/limitations, liquidity requirements and other regulations involving the operationalization of the investment objectives, investment policy or strategy of the Investment Company;
5. Oversee the transactions of the Fund Manager to ensure that delegation will not result in unnecessary fees to be paid by the Investment Company and ensure that it will not delegate its function to the extent that it becomes a letter box such as when it no longer has the power to take decisions in the implementation of the investment policy and strategies nor retain the suitable processes to monitor, control the activities and evaluate the performance of the delegatee;
6. If, in the reasonable opinion of the IOE, the Fund Manager has not complied with any of the laws, rules or regulations applicable to the Investment Company and/or it failed to report to the Commission the said non-compliance, notify the Commission of its opinion, including particulars of the non-compliance, not later than five (5) business days after forming the opinion or upon knowledge of the non-compliance. The notification shall be done by filing an SEC Form 17-C. It shall also notify, without delay, the members of the Board of Directors of the Investment Company of its opinion so that the Board can apprise the Fund Manager of the said non-compliance and address any resulting breach;
7. Report to the Commission, any act of the Fund Manager which in its opinion may be detrimental to the interests of the shareholders or unitholders even if the said act is not in violation of any law, rule or regulation, not later than five (5) business days from knowledge thereof; and
8. If necessary, recommend to the Board of Directors of the Investment Company that the Fund Manager be removed due to its inability to fulfill its functions.

D. Penalties

A. For failure of the IOE to comply with any of its responsibilities, the penalty shall be:

Description	First Violation	Second Violation	Third Violation	Fourth violation
Failure to comply by the Audit Committee as IOE	Reprimand	₱20,000.00	₱50,000	Disqualification of the erring member as a director of the concerned Investment Company, Fund Manager and such other Funds managed by the same Fund Manager for a period of two (2) years from disqualification
Failure to comply by the Custodian Bank, Trust Entity or	Reprimand	₱20,000.00	₱50,000	Disqualification of the erring entity to act as IOE for all Investment Companies for a period of two (2)

External Auditor as IOE				years from disqualification

In the case of an Audit Committee serving as IOE, all members of the Audit Committee shall be jointly and severally liable for the monetary penalty mentioned above. Each member is liable for the entire obligation but he/she who made the payment may reimburse or claim from his/her co-members the share which corresponds to each.

B. Failure to comply by the Fund Manager to provide the necessary assistance required by the IOE to enable it to perform its functions shall be subject to the following:

i. Basic Penalty: ₱50,000.00
ii. Monthly Penalty: ₱5,000.00

The monthly penalty shall accrue until the necessary assistance has been provided.

C. The appointment of an unqualified entity or member of the Audit Committee as IOE shall subject the Investment Company to the following:

i. Basic penalty: ₱20, 000.00
ii. Monthly penalty: ₱2,000.00

The monthly penalty shall accrue until the appointment of a qualified member of the Audit Committee.

D. The continuous non-compliance with the requirements of these Rules shall constitute a ground for the imposition of penalties provided under the Securities Regulation Code (SRC), Revised Corporation Code (RCC), and their Implementing Rules and Regulations (IRR), such as suspension and revocation of the subject entity's registration and/or secondary licenses.

II. Independent Net Asset Value Calculation

A. An Investment Company is required to engage an independent entity that will calculate or cross-check its Net Asset Value (NAV) every dealing day which may be the custodian bank, trust entity, external auditor, audit committee or other service providers capable of calculating the NAV.

To be considered independent, the following criteria must be met:

1. The Custodian Bank or Trust Entity must be duly licensed by the Bangko Sentral ng Pilipinas, provided that it does not hold directly/indirectly 10% or more of the total number of issued shares in the Investment Company, Fund Manager, or vice versa, nor have a common shareholder that holds directly/indirectly 10% or more of the total number of the issued share capital of the Investment Company or Fund Manager; and

2. The External Auditor shall not be the same as the one auditing the Investment Company and Fund Manager.

An Investment Company may engage for this purpose its Audit Committee acting as IOE, provided that it is capable of calculating the NAV, and other service providers

capable of calculating the NAV, provided that they are not affiliated with the Investment Company and Fund Manager.

B. An Investment Company, or the Fund Manager authorized by the former, who fails to appoint an independent entity that will calculate or cross-check the investment company's NAV every dealing day shall be subject to a basic penalty of Fifty Thousand Pesos (₱50,000.00) and a monthly penalty of Five Thousand Pesos (₱5,000.00). The monthly penalty shall accrue until the Investment Company, or the authorized Fund Manager, appoints said independent entity. This is without prejudice to other administrative sanctions which may be imposed by the Commission.

The Investment Company is deemed to have failed to appoint the required independent entity and shall be subject to the same penalty upon discovery of the Commission that the Audit Committee or other service providers appointed are not capable of calculating the NAV.

III. Professional Qualifications of Key Officers Responsible for Making Investment Decisions

All Fund Managers of Investment Companies, which offer products either domestically or under a cross-border agreement, must comply with the professional qualifications requirements of key officers responsible in making investment decisions. The provisions of ICA Rule 5.1.1 (i) are hereby amended to read as follows:

i. Key officers, who are responsible for making investment decisions shall have any of the following qualifications:

i. At least a Bachelor's degree, or its equivalent; completed a Certification or Professionalization program on fund management and/or relevant program or training recognized globally or locally and acceptable to the Commission; and at least three (3) years of experience within the past five (5) years in fund management and/or related functions;

ii. Professional qualifications; completed a certification or professionalization program on fund management and/or other relevant program or training recognized globally or locally and acceptable to the Commission; and at least five (5) years of experience within the past seven (7) years in fund management and/or related functions; or

iii. If a qualified professional is appointed on a non-permanent basis: at least five (5) years of experience within the past seven (7) years in fund management and/or related functions; in lieu of professional qualifications, must have completed a certification or professionalization program or training recognized globally or locally and acceptable to the Commission; and obtained a prior approval from the Commission of his engagement as such.

The Commission shall be notified of the appointment or official engagement of the said key officer, through SEC Form ICA-IA, within five (5) days from appointment or official engagement, whichever is earlier. The same procedure and form shall also be applied in cases of disengagement/resignation of said key officer.

The Commission may prescribe a licensure exam which would replace the above-required certification or professionalization program on fund management and/or other relevant program or training.

IV. Liquidation of Assets and Winding up of the Investment Company

All Investment Companies, regardless of whether it transacts under cross-border agreements or not, shall ensure compliance with these rules on winding up.

The Fund Manager shall carry out the liquidation of assets on behalf of the Investment Company. In all cases of revocation of the Registration Statement and Certificate of Permit to Offer Securities for Sale, the Fund Manager must liquidate the assets within a maximum period of six (6) months from the receipt of the Investment Company of the Order revoking the Registration Statement and its Certificate. The Investment Company must wind up or amend its business purposes within one (1) year from receipt of the same.

In addition to the requirement of Rule 13.1.8 of the ICA IRR, the Fund Manager shall file a monthly report with the Commission, within ten (10) days after the end of every month, on the redemption of securities in the immediately preceding month. The report shall include the following:

1. Number of shares redeemed;
2. Number of shareholders or unitholders whose securities were redeemed;
3. Number of shareholders or unitholders whose securities are yet to be redeemed; and
4. The reasons why their securities are not yet redeemed.

In cases specified under Rules 5.1.10 and 13.1.2 (d) of the ICA IRR, where the Commission appoints a liquidator to facilitate the liquidation of assets, the liquidator shall be the one to file the report as specified above.

The failure of the Fund Manager or the liquidator to comply with any of the foregoing requirements shall subject it to a basic penalty of Twenty Thousand Pesos (₱20,000.00) for each violation and a monthly penalty of Five Thousand Pesos (₱5,000.00). The monthly penalty shall continue to accrue until the report is completed.

As to the redemption of funds, the Fund Manager or the liquidator may appoint a Transfer Agent or a Custodian Bank, who will act a disbursing agent for the redeemed shares/units. The appointed Transfer agent or Custodian Bank must be in operation for at least five (5) years.

V. Transitory Provision and Effectivity

This Circular shall take effect within fifteen (15) days after its publication in two (2) newspapers of general circulation. The compliance with the Rules may be deferred by the Commission provided that the deferment shall not exceed more than **six (6) months** from the effectivity date.

Pasay City, Philippines. Sept. 24 2019.

For the Commission:

EMILIO B. AQUINO
Chairperson