Republic of the Philippines
SECURITIES AND EXCHANGE COMMISSION
SEC Building, EDSA, Greenhills, Mandaluyong City, Metro Manila

SEC MEMORANDUM CIRCULAR NO. 16
Series of 2004

TO: ALL BROKERS DEALERS
PHILIPPINE STOCK EXCHANGE

SUBJECT: ADOPTION OF THE RISK BASED CAPITAL ADEQUACY REQUIREMENT/RATIO (RBCA) FOR BROKERS DEALERS

The Commission, pursuant to its regulatory and supervisory powers under Section 5 of the Securities Regulation Code (SRC), approved the following guidelines on the adoption in the Philippines of the Risk Based Capital Adequacy (RBCA) Framework for all registered Brokers Dealers in accordance with SRC Rule 28.1 (E) (2) (iv) of the SRC. These guidelines shall cover the following risks: (1) Position or Market Risk, (2) Credit Risks such as Counterparty Risk, Settlement Risk, Large Exposure Risk, and Margin Financing Risk, and (3) Operational Risk.

PART I: PRUDENTIAL AND FINANCIAL MEASURES

RULE 49.1 (A) PAID UP CAPITAL REQUIREMENT

Unless otherwise prescribed by the Commission, the paid-up capital of every Broker Dealer covered by the RBCA shall be governed by the existing requirements of SRC Rule 28.1 (E) (v).

For this purpose, the term "paid up capital" shall include the following:

a. Capital contributions of partners or par value or stated value of Common Stock
b. Payment made on Subscribed Common Stock

c. Par or Stated Value of Preferred Stock
d. Payment made on Subscribed Preferred Stock
e. Common Stock to be Distributed (arising from a Stock Dividend Declaration)
f. Additional Paid in Capital for both Common and Preferred Stocks
g. Donated Capital

The value representing Treasury Stock is deducted in the computation of Paid up capital.

RULE 49.1 (B) RESERVE FUND

(1) Every Broker Dealer shall annually appropriate a certain minimum percentage of its audited profit after tax and transfer the same to the Appropriate Retained Earnings Account in accordance with the following schedule:

Unimpaired Paid Up Capital PhP (million)	**Minimum percentage or profit after tax to be placed in the Appropriated Retained Earnings**
Between 10-30	30%
Between 30- 50	20%
More than 50	10%

(2) The amount appropriated shall not be available for payment of dividends.
(3) Where in any financial year the Broker Dealer's paid up capital is impaired, the Broker Dealer, is required to transfer from the Appropriated Retained Earnings to the capital account an amount equivalent to the impairment. Such amount so transferred out shall not be available for payment of dividend.
(4) Consistent with the general usage under SRC Rule 28.1 (E) (v), the term "Unimpaired Paid Up Capital" shall refer to the firm's Total Paid Up Capital less any deficiency in the Retained Earnings account.
(5) A Broker Dealer may submit to the Commission for approval its own capital build up plan in lieu of the requirements of this provision.
(6) Notwithstanding the requirements of this section, the Commission may prescribe a different capital build up plan for all Broker Dealers, specifically those incurring net losses during the period, with may include the programmed infusion of fresh capital.

RULE 49.1 (C) RESERVE REQUIREMENT ACCOUNT AND CUSTODY OF SECURITIES

Unless otherwise prescribed by the Commission, the responsibilities related to the setting up of a Reserve Requirement Account by every Broker Dealer and the custody of securities shall be governed by the requirements of SRC Rule 49.2 (Customer Protection Reserves and Custody of Securities) and shall be observed at all times.

PART 2 FINANCIAL RECORDS AND REPORTING

Financial Records and Reporting shall be primarily governed by SRC Rule 52.1 (Accounts and Records, Reports, Examination of Exchanges, Members and Others) and secondarily by all pertinent provisions of the SRC and its Implementing Rules, and all other regulations which the Commission may from time to time adopt.

With respect to compliance with the requirements on RBCA, every Broker Dealer covered by the RBCA rules shall prepare its RBCA Report as of month end and file the same with the Commission on or before the 15th of the following month. The RBCA Report shall be certified by the firm's Associated Person and President/Nominee Director and a copy submitted to the Broker Dealer's Audit Committee or in lieu thereof, its Board of Directors. A pro-forma RBCA Report to be prescribed by this Commission shall form part of this Rule.

In situations where any of the financial obligations of Broker Dealers as prescribed under Part 6 Subsection II is breached, the Associated Person must immediately notify the Commission, the Exchange, and the company's Board of Directors. Proper corrective measures must be adopted by the Board to avoid suspension of operations. Daily notification by the Broker Dealer is required to the Commission and the Exchange until the breach is fixed or corrected.

In compliance with the requirements of SRC Rule 52.1 (5) (Annual Audited Financial Reports of Broker Dealers), every Broker Dealer shall, in lieu of submitting a Computation of Net Capital under SRC Rule 49.1, submit the RBCA Report.

PART 3 RISK MANAGEMENT AND INTERNAL CONTROL

RULE 49.1 (D) PRINCIPLES OF RISK MANAGEMENT

(1) Every Broker Dealer shall -

(a) establish, maintain and exercise effective policies and procedures on risk management; and

(b) have its own system of monitoring risk on a daily basis.

The Broker Dealer should be able to describe and demonstrate the objectives and operation of the system to the Exchange and the Commission. The policies and procedures on risk management shall be documented in a Risk Management Manual. Said manual shall be periodically updated to effect certain changes in the system. A certification from the management of the Broker Dealer that the Risk Management procedures have been consistently followed should be submitted to the Commission and the Exchange.

(2) Every Broker Dealer shall determine and record in its financial records appropriate position and credit limits for all counterparties to which it has a credit exposure.

(3) The position and credit limits established shall be appropriate to the type, nature and volume of business undertaken and the financial status of the counterparty and shall be reviewed on a regular basis, at least once a year. Every Broker Dealer shall be responsible in determining the propriety of conducting more frequent reviews taking into consideration the changes in the financial condition of its counterparties.

(4) A Broker Dealer's financial records shall be capable of being summarized in such a way as to permit actual exposures to be measured regularly against the established position and credit limits.

(5) A Broker Dealer shall maintain its records in a manner such that they adequately disclose, or are capable of adequately disclosing, in a prompt and appropriate manner, the financial and business information which will enable its management to -

(a) identify, quantify, control and manage the Broker Dealer's risk exposures;

(b) make timely and informed decisions;
(c) monitor the performance of all aspects of the Broker Dealer's business on an up-to-date basis;
(d) monitor the quality of the Broker Dealer's assets; and
(e) safeguard the assets of the Broker Dealer and assets belonging to other persons for which the Broker Dealer is responsible.

(6) Every Broker Dealer's risk systems and processes should be capable of being externally and independently audited by the Exchange, Commission or any other third party acting on behalf of the Exchange or the Commission..

RULE 49.1 (E) INTERNAL CONTROL

(1) Every Broker Dealer shall establish and maintain at all times written policies and procedures on internal control and should be able to describe and demonstrate the objectives and operation of such policies and procedures to the Exchange and the Commission.

(2) In determining the scope and nature of effective internal control, a Broker Dealer shall consider all relevant factors including the size of the business, the diversity of operations, the volume, size and frequency of transactions, the degree of risk associated with each area of operation and the amount of control by its senior management over day to day operations.

(3) The systems of internal control shall be designed in such a way as to ensure that -

(a) all transactions and commitments entered into are recorded and are within the scope of authority of the Broker Dealer or the individual acting on behalf of the Broker Dealer entering into such transactions or commitments;
(b) there are procedures to safeguard assets and control liabilities, including assets belonging to other persons for which the Broker Dealer is accountable;
(c) there are measures, so far as is reasonably practicable, to minimise the risk of losses to the Broker Dealer from irregularities, fraud or error and to identify such matters should they occur so that prompt remedial action may be taken by the management;
and
(d) there is clear delineation of responsibilities and proper segregation of tasks among the departments and the personnel of the Broker Dealer.

PART 4 PROVISIONING FOR OVERDUE ACCOUNTS

RULE 49.1 (F) PROVISIONS FOR OVERDUE ACCOUNTS

A. Definitions

For purposes of implementing the requirements of this section, the following terms shall have their respective meanings:

- **Amount outstanding** – with respect to a particular customer account, refers to the total or aggregate receivable or collectible due from any account at any one time, inclusive of commission charges, interest charges and other relevant and reasonable charges).
- **Contra losses** – refers to all losses incurred by customers arising from contra transactions, inclusive of relevant and reasonable charges.
- **Contra transaction** – refers to a transaction where a Broker Dealer allows its client to settle outstanding buy positions against outstanding sell positions of the same securities where the orders for both buy and sell orders are made within the same period stipulated by the Commission. Unless another period is prescribed by the Commission, the period referred to is the same trading day.
- **Effective date** – refers to the effectivity date of the guidelines.
- **Equity** – refers to the client's/customer's required equity maintenance in the form of cash and securities needed for purposes of opening a margin account with the Broker Dealer
- **Interest** – refers to all charges and fees payable by the customer to the Broker Dealer arising from a legal loan agreement or any similar arrangement.
- **Interest-in-suspense** – refers to the interest that has been suspended and credited to the interest-in-suspense account in accordance with these rules.
- **Interest-in-suspense account** – refers to the account so designated for the interest-in-suspense.
- **Margin account** – refers to the account opened and maintained by a customer for the purpose of trading securities pursuant to credit facilities extended by the Broker Dealer to the customer as evidenced by a formal agreement entered into by both parties
- **Non-performing account** – refers to customer accounts which have remained outstanding for a relatively long period as qualified under *Schedule for Part 4*

(found at the end of these Rules) and which requires specific and general provisioning for possible uncollectibility.

- **Overdue purchase contract** refers to a buy contract for securities which is outstanding and for which no mandatory close out could be implemented due to the following reasons:
    - i. Securities giving rise to the outstanding position have been suspended from trading by the Exchange or the Commission;
    - ii. There is no ready market;
    - iii. Such other circumstances or causes acceptable to the Commission or upon recommendation of the Exchange.

B. Provisioning for Overdue Accounts

1. Consistent with SRC Rule 52.1 (Accounts and Records, Reports, Examination of Exchanges, Members and Others) subsection 11 (on Monthly Aging of Accounts Receivable), every Broker Dealer shall provide for Specific and General Provisions for overdue accounts on all non-performing customer accounts.

2. Unless otherwise prescribed by the Commission, every Broker Dealer shall comply with these guidelines in the preparation of its RBCA report and audited financial statements.

3. Specific and General Provisions for Overdue Accounts shall be computed in accordance with the *Schedule for Part 4 (found at the end of these Rules).*

4. Every Broker Dealer must establish its own policies on the writing off of bad debts and these policies must be consistent with Generally Accepted Accounting Principles (GAAP). International Accounting Standards (IAS) may be resorted to in cases whether there are no applicable Philippine GAAP that addresses the issue. The Broker Dealer, within seven (7) days after effecting the write off, is required to disclose the same to the Commission and Exchange provide specific details on these written off accounts of single clients where such amounts singly or in aggregate exceeds P500,000.

PART 5 SATISFACTORY SUBORDINATION AGREEMENTS

RULE 49.1 (G) SUBORDINATED LIABILITIES

A. i. This rule sets forth minimum and non-exclusive requirements for satisfactory subordination agreements (hereinafter "subordination agreement"). The Exchange, Commission, or Broker Dealer may require or include such other provisions as may be deemed necessary to the extent that such provisions do not cause the subordination agreement to fail to meet the minimum requirements of this Rule.

The subordinated agreement shall be approved by the Exchange, if affecting an Exchange Member, or by the Commission, if affecting a non-Exchange Member. Said agreement shall take effect upon such approval.

ii. For purposes of SRC Rule 49.1 (G):

a. A subordination agreement may be either a subordinated loan agreement or a secured demand note agreement.

b. "**Subordinated loan agreement"** shall mean a notarized agreement evidencing or governing a subordinated borrowing of cash.

c. The "**Collateral Value"** of any securities pledged to secure a secured demand note shall mean the market value of such securities after reducing the market value of the securities by the position risk requirements as provided in Subsection V below.

d. "**Payment Obligation"** shall mean the obligation of a Broker Dealer in respect of any subordination agreement (i) to repay cash loaned to the Broker Dealer pursuant to a subordinated loan agreement or, (ii) to return a secured demand note contributed to the Broker Dealer or reduce the unpaid principal amount thereof and to return cash or

securities pledged as collateral to secure the secured demand note. "**Payment**" shall mean the performance by a Broker Dealer of a Payment Obligation.

e. (1) **Secured demand note agreement** shall mean a notarized agreement (including the related secured demand note) evidencing or governing the contribution of a secured demand note to a Broker Dealer and the pledge of securities and/or cash with the Broker Dealer as collateral to secure payment of such secured demand note. The secured demand note agreement may provide that neither the lender, his heirs, executors, administrators or assigns shall be personally liable on such note and that, in the event of default, the Broker Dealer shall look for payment of such note solely to the collateral then pledged to secure the same.

(2) The secured demand note shall be a promissory note executed by the lender and shall be payable on the demand of the Broker Dealer to which it is contributed; provided, however, that the making of such demand may be conditioned upon the occurrence of any of certain events which are acceptable to the Commission and to an Exchange in the case of a Broker Dealer which is a member of that Exchange.

(3) If such note is not paid upon presentment and demand as provided for therein, the Broker Dealer shall have the right to liquidate all or any part of the securities then pledged as collateral to secure payment of the same and to apply the net proceeds of such liquidation, together with any cash then included in the collateral, in payment of such note. Subject to the prior rights of the Broker Dealer as pledgee, the lender, as defined herein, may retain ownership of the collateral and have the benefit of any increases and bear the risks of any decreases in the value of the collateral and may retain the right to vote securities contained within the collateral and any right to income therefrom or distributions

thereon, except the Broker Dealer shall have the right to receive and hold as pledgee all dividends payable in securities and all partial and complete liquidating dividends.

(4) Subject to the prior rights of the Broker Dealer as pledgee, the lender may have the right to direct the sale of any securities included in the collateral, to direct the purchase of securities with any cash included therein, to withdraw excess collateral or to substitute cash so other securities as collateral, provided that the net proceeds of any such sale and the cash so substituted and the securities so purchased or substituted are held by the Broker Dealer, as pledgee, and are included within the collateral to secure payment of the secured demand note, and provided further that no such transaction shall be permitted if, after: giving effect thereto, the sum of the amount of any cash, plus the Collateral Value of the securities, then pledged as collateral to secure the secured demand note would be less than the unpaid principal amount of the secured demand note.

(5) Upon payment by the lender, as distinguished from a reduction by the lender which is provided for in "Annex 49.1-2A" paragraph 6(C) or reduction by the Broker Dealer as provided for in "Annex 49.1-2A" paragraph (b)(7) of the Implementing Rules and Regulations of the SRC, of all or any part of the unpaid principal amount of the secured demand note, a Broker Dealer shall issue to the lender a subordinated loan agreement in the amount of such payment (or in the case of a Broker Dealer that is a partnership credit a capital account of the lender) or preferred or common stock(s) of the Broker Dealer in the amount of such payment, or any combination of the foregoing, as provided for in the secured demand note agreement.

f. **"Lender"** shall mean the person who lends cash to a Broker Dealer pursuant to a subordinated loan agreement

and the person who contributes a secured demand note to a Broker Dealer pursuant to a secured demand note agreement.

B. Recourse to the Subordination Agreements is viewed as a temporary relief to address RBCA requirements of Broker Dealers and is not intended to replace the permanent infusion of capital by stockholders. Thus, subordinated loans shall be for a maximum period of four (4) years or for such longer period as the Commission deems appropriate, provided however, that a capital buildup plan shall be a requirement for the approval of the subordinated loan. Advances or Agreements that have been outstanding for more than four (4) years would require conversion to capital unless, during the life of the subordinated loan, an equivalent infusion of capital by way of investment is made or earnings have accumulated to an equivalent amount by reason of profitable operations, in which case compulsory conversion of the debt to equity can be dispensed with upon prior application with and approval by the Commission.

C. In order to ensure financial viability of the Broker Dealer, the Exchange, for Exchange Broker Dealers, or the Commission, for non-Exchange Broker Dealers, may impose additional requirements to regulate the resort to financing by way of subordination agreements and may exercise discretion in the approval of such agreements.

D. The Minimum requirements for Subordination Agreements and Miscellaneous Provisions and the sample format of the Subordinated Loan Agreement are set forth in Annex 49.1-2A and Annex 49.1-2A respectively, of the Implementing Rules and Regulations of the SRC.

PART 6 RISK BASED CAPITAL ADEQUACY REQUIREMENTS

RULE 49. 1 (H) RISK BASED CAPITAL ADEQUACY RATIO REQUIREMENTS (RBCA)

Subsection I. DEFINITION AND INTERPRETATION

A. DEFINITION

- **Adequately secured indebtedness** shall be deemed to exist when the excess of the market value of the collateral over the amount of the indebtedness is sufficient to make the loan acceptable as a fully secured loan to banks regularly making secured loans to Broker Dealers.

- **Aggregate Indebtedness** shall mean the total money liabilities of a Broker Dealer arising in connection with any transaction whatsoever, and includes, among other things, money borrowed, money payable against securities loaned and securities failed to receive, the market value of securities borrowed to the extent to which no equivalent value is paid or credited (other than the market value of margin securities borrowed from customers and margin securities borrowed from non-customers), customers' and non-customers' free credit balances, and credit balances in customers' and non-customers' accounts having short positions in securities, but excluding:

  i. Indebtedness adequately collateralized by securities which are carried long by the Broker Dealer and which have not been sold or by securities which collateralize a secured demand note in conformity with SRC Rule 49.1 (G) above;

  ii. Amounts payable against securities loaned, which securities are carried long by the Broker Dealer and which have not been sold or which securities collateralize a secured demand note in conformity with SRC Rule 49.1 (G) above;

  iii. Amounts payable against securities failed to receive which securities are carried long by the Broker Dealer and which have not been sold or which securities collateralize a secured demand note in conformity with SRC Rule 49.1 (G) above; or amounts payable against securities failed to receive for which the Broker Dealer also has a receivable related to securities of the same issue and quantity thereof which are either fails to deliver or securities borrowed by the Broker Dealer;

  iv. Fixed liabilities adequately secured by assets acquired for use in the ordinary course of the trade or business of a Broker Dealer but not other fixed liabilities secured by assets of the Broker Dealer shall be so excluded unless the sole recourse of the creditor for nonpayment of such liability is to such asset;

v. Indebtedness subordinated to the claims of creditors pursuant to a satisfactory subordination agreement in conformity with SRC Rule 49.1 (G) above;

vi. Liabilities which are effectively subordinated to the claims of creditors, but which are not subject to a satisfactory subordination agreement in conformity with SRC Rule 49.1 (G) above; by non-customers of the Broker Dealer prior to such subordination, except such subordinations by customers as have been approved by an Exchange in the case of a member of that Exchange and the Commission in the case of a firm that is not a member of an Exchange;

vii. Credit balances in accounts of general partners;

viii. Deferred tax liabilities; and

ix. Eighty percent (80%) of amounts payable against securities loaned for which the Broker Dealer has receivables related to securities of the same class and issue and quantity that are securities borrowed by the Broker Dealer.

- **Asset or Market Liquidity Risk** means that risk that an entity will be unable to unwind a position in a financial instrument at or near its market value because of the lack of depth or disruption in the market for that instrument.

- **Broker Dealer, Broker or Dealer** – shall refer to any Broker and/or Dealer registered by the Commission under the Securities Regulation Code and its implementing rules and regulations.

- **Commission** means Securities and Exchange Commission or SEC

- **Core Equity**– shall refer to the sum of:
  i. Paid-up common stock;
  ii. Paid-up perpetual and non-cumulative preferred stock
  iii. Common stock dividends distributable
  iv. Perpetual and non-cumulative preferred stock dividends distributable;
  v. Additional paid in Capital (also known as Surplus);
  vi. Surplus reserves excluding revaluation reserves or appraisal capital;

vii. Opening retained earnings adjusted for all current year movements

Provided, further, That the following items shall be deducted from the Total of Core Equity:

(1) Common stock treasury shares
(2) Perpetual and non-cumulative preferred stock treasury shares;
(3) Unbooked valuation reserves and other capital adjustments (such as unrealized gain in value of non-current investments)

- **Counterparty** means any person or entity with or for whom a Broker Dealer carries on, or intends to carry on, any dealings in securities or another asset which could be either another executing Broker Dealer or a client.

- **Counterparty Risk** means the risk of a counterparty defaulting on its financial obligation to a Broker Dealer.

- **Counterparty Risk Requirement** – means the amount necessary to accommodate a given level of its Counterparty Risk, as calculated in accordance with Subsection VI.

- **Customer** shall mean any person from whom, or on whose behalf, a Broker Dealer received, acquired or holds funds or securities for the account of such person, but shall not include a general, special or limited partner or director or officer of the Broker Dealer, or any person to the extent that such person has a claim for property or funds which by contract, agreement or understanding, or by operation of law, is part of the capital of the Broker Dealer or is subordinated to the claims of creditors of the Broker Dealer. However, the term "customer" of a Broker Dealer shall include another Broker Dealer (the initiating Broker as defined in SRC Rule 34.1 wherein the latter maintains separately a Dealer account and a special omnibus account in behalf of his customer with the former.

- **Debt or Liability -** means borrowed funds represented by a security, instrument or public document that must be repaid by the Broker Dealer, issuer, or debtor.

- **Debt securities** – means securities other than equity securities which may be any of the following or of a similar nature:

i. A debt security without call or put provisions;
ii. A discounted security without call or put provisions;
iii. A non-convertible preferred share;
iv. A redeemable preferred share with a fixed and certain date for redemption;
v. An interest in a managed collective investment scheme investing only in debt or fixed income securities, mortgages, or cash;
vi. Any other instrument defined as such by the Commission.

- **Equity per Books (also called Net Worth)**–refers to the Total Stockholders' Equity section of the Balance Sheet computed as the difference between the book values of Total Assets and Total Liabilities.

- **Equity Eligible for Net Liquid Capital** - shall refer to the Equity as per Books adjusted for all other liabilities which in substance can be treated as sources of capital, less ineligible equity items, the computation of which is described in Subsection III below.

- **Equity Securities-** means securities other than debt securities which may be any of the following or of a similar nature:

  i. A share other than those referred to in paragraphs (iii) and (iv) of the definition of Debt securities;
  ii. A depository receipt;
  iii. An installment receipt;
  iv. An interest in a managed collective investment scheme other than an interest referred to in paragraph (e) of the definition of Debt securities;
  v. An instrument defined as such by the Commission;

- **Exchange Traded** – means traded or listed on a Registered Exchange

- **Funding Liquidity Risk** means the risk that an entity cannot obtain the necessary funds to meet its obligations as they fall due at normal times and during a crisis.

- **General Guarantees** – shall refer to general guarantees of indebtedness and acceptances (including endorsements with the character of acceptances) made by the Broker Dealer for loans or indebtedness incurred or assumed by a person/individual or entity other than the Broker Dealer himself.

- **Indebtedness Subordinated to the claims of Creditors** – refers to subordinated liabilities as provided under Part 5 (Satisfactory Subordination Agreements) above.

- **Large Exposure Limit** – Means the maximum permissible large exposure and calculated as a percentage of Core Equity in accordance with Subsection VII.

- **Large Exposure Risk** – means risks to which a Broker Dealer is exposed whether by way of:

  a. a proportionally large amount of exposure to a particular counterparty;
  b. a proportionally large exposure to a single issuer of debt;
  c. a proportionally large exposure to a single equity security or single issuer group;

- **Large Exposure Risk Requirement** – means the amount necessary to accommodate a given level of the Broker Dealer's Large Exposure Risk, which is in excess of the Large Exposure Limit.

- **Liquid Assets**– means securities or other assets which have a ready market which are realizable or capable of being converted into cash within 30 days.

- **Liquid Securities**- means securities which have a ready market as defined herein below.

- **Marked to Market** – is a securities valuation method where securities are valued at their closing prices on a market day.

- **Net Liquid Capital (also called NLC)** shall mean the Equity Eligible for Net Liquid Capital of a Broker Dealer, adjusted for non-allowable current and non-current assets as described in Subsection III below.

- **Operational Risk** –is the exposure associated with commencing and remaining in business arising separately from exposures covered by other risk requirements. It is the risk of loss resulting from inadequate or failed internal processes, people and systems which include, among others, risks of fraud, operational or settlement failure and shortage of liquid resources, or from external events.

- **Operational Risk Requirement-** means the amount calculated in accordance with Subsection IV which is required to cover a level of Operational Risk.

- **Position Risk (also called Market Risk)-** is the risk to which a Broker Dealer is exposed to and arising from securities held by it as a principal or in its proprietary or dealer account.

- **Position Risk Requirement (also called Market Risk Requirement)** - means the amount necessary to accommodate a given level of Position Risk (also called Market Risk), as calculated in accordance with Subsection V.

- **Ready market** – means a recognized established securities market in which exists independent bona fide offers to buy and sell so that a price reasonably related to the last sales price or current bona fide competitive bid and offer quotations can be determined for a particular security almost instantaneously and where payment will be received in settlement of a sale at such price within a relatively short time. Notwithstanding the above definition, the Commission may declare a certain security as not having a ready market on the basis of historical trading volume.

  A **Ready market** shall also be deemed to exist where securities have been accepted as collateral for a loan by a bank and where the Broker Dealer demonstrates to an Exchange in the case of a member of that Exchange or the Commission in the case of a firm that is not a member of an Exchange that such securities adequately secure such loans.

- **Risk Based Capital Adequacy Ratio (also called RBCA Ratio)**– means the ratio linking the net liquid capital to the Broker Dealer's total risk exposure (Total Risk Requirement), calculated as the Broker Dealer's Net Liquid Capital (NLC) divided by its Total Risk Capital Requirement (TRCR).

- **Total Risk Capital Requirement (TRCR)** is the sum of:

  A. Operational Risk requirement
  B. Credit Risk Requirement which include requirements for Counterparty Risk, Settlement Risk, Large Exposure Risk, and Margin Lending/Financing Risk
  C. Position or Market Risk Requirement

- **Securities Borrowing and Lending** refers to any transaction by the Broker Dealer under an equity or debt security lending and borrowing agreement, a repurchase or reverse repurchase agreement or an agreement for the sale and buyback of the security or other similar agreement as prescribed by the Exchange and duly approved by the Commission and, subject to appropriate tax laws, by the Bureau of Internal Revenue.

B. INTERPRETATION

The RBCA Rules should be applied and understood in relation to the Securities Regulation Code (SRC) and its implementing rules and regulations. In case of doubt, the RBCA rules should be interpreted in a manner that is consistent with the SRC and its implementing rules and regulations and international best practices in financial services regulation. When in need of policy direction or legal interpretation, the Broker Dealer must seek guidance from the Commission's Market Regulation Department. In choosing the appropriate treatment of financial transactions which impact on the RBCA computation, the choice should be that which would provide a more conservative computation of RBCA ratio.

Subsection II. OBLIGATIONS OF BROKER DEALERS

A. General Obligations:

1. Every Broker Dealer shall ensure that:

   a. Its Risk Based Capital Adequacy Ratio is greater than or equal to 1.1.

   b. Its Core Equity is at all times greater than its Operational Risk Requirement. In case of breach, the Broker Dealer shall be allowed to continue it operations provided that it shall submit a capital build plan which should be realized within ninety (90) calendar days from time of breach.

   c. The Special Reserve Bank Account created for the Exclusive Benefit of Customers shall be maintained by the Broker Dealer as prescribed under SRC Rule 49.2 (Customer Protection Reserves and Custody of Assets) and mentioned in Part I (Rule 49.C) of this Rule. Qualified Securities maintained in the Reserve Custody Account pursuant to the said SRC Rule shall be subject to the appropriate position risk requirement.

d. Every Broker Dealer shall, at all times, have and maintain a NLC of at least Five Million Pesos (P5,000,000.00) or five percent (5%) of his aggregate indebtedness whichever is higher. However, a Broker Dealer who deals only with proprietary shares and who does not keep the shares under its custody shall have and maintain a net capital of P2.5 Million Pesos or two and one-half percent (2.5%) of his aggregate indebtedness, whichever is higher. In cases where, in order to meet the RBCA ratio of at least 1.1, an NLC higher than Five Million Pesos (P5,000,000) or five percent (5%) of aggregate indebtedness is required, the higher NLC shall be maintained.

The Commission may prescribe a lower or higher minimum NLC depending on the effectiveness of the risk management systems adopted by Broker Dealers, their ability to instantaneously respond to various risks as a result of daily monitoring and reporting on capital adequacy levels, and other developments in the market that would impact on the risk exposure levels of the firms.

e. In computing position (or market) and counterparty risk exposures, all assets shall be marked to market daily.

2. Notwithstanding the monthly reporting to be made to the Commission and the Exchange on its RBCA as of month end, every Broker Dealer shall compute its Net RBCA Margin and RBCA Ratio on a daily basis and these working papers will form part of the Books and Records of the firm. The Commission or an Exchange, in the case of a member of an Exchange, may require Broker Dealers from time to time to submit reports which reflect their RBCA Ratio and Margin. In such cases, the Broker Dealer shall immediately submit said reports to the Exchange or the Commission.

3. Every Broker Dealer shall immediately cease doing business as a Broker Dealer, and shall notify the Exchange and the Commission if (i) the minimum Risk Based Capital Adequacy Ratio of 1.1 or (2) the minimum NLC is breached.

B. No Broker Dealer shall permit its aggregate indebtedness to all other persons to exceed 2,000 percent of its NLC.

C. Notwithstanding the requirement in paragraphs A & B above, every Broker Dealer shall notify the Commission in writing within twenty four (24) hours, the occurrence of any of the following events:

i. The Broker Dealer's computation shows that its Aggregate Indebtedness is in excess of 1,700 percent of its NLC; and /or

ii. The Broker Dealer's computation shows that its Risk Based Capital Adequacy Ratio is less than 1.2; or

The Broker Dealer shall, upon immediate notification, take all necessary action to increase its NLC or reduce its total risk exposure. The Exchange, upon prior consultation with the Commission, or the Commission may, after receipt of such notice, direct the Broker Dealer in its conduct of its operations and/or impose conditions, if necessary.

The Broker Dealer is given ten (10) calendar days within which to effect its proposal. Pending actual implementation, the Broker Dealer is required to notify the Commission on a daily basis of its NLC position.

D. LIMITATIONS ON WITHDRAWAL OF CORE EQUITY

i. No equity capital of a Broker Dealer may be withdrawn by action of a stockholder or a partner or by redemption or repurchase of shares of stock or through the payment of dividends or any similar distribution, nor may any unsecured advance or loan be made to a stockholder, partner, sole proprietor, employee or affiliate, if after giving effect thereto and to any other such withdrawals, advances or loans and any payments under satisfactory subordination agreements in conformity with SRC Rule 49.1 (G) above which are scheduled to occur within one hundred and eighty (180) days following such withdrawal, advance or loan if:

a. The Broker Dealer's NLC would be less than one hundred twenty percent (120%) of the minimum amount required by paragraph (A) of this rule; or,

b. The aggregate indebtedness of the Broker Dealer exceeds one thousand five hundred percent (1500%) of its net capital.

ii. This, however, shall not preclude a Broker Dealer from making required tax payments or preclude the payment to partners of reasonable compensation, and such payments shall not be included in the calculation of withdrawals, advances, or loans for purposes of paragraph D above.

iii. For the purpose of this section, any transaction between a Broker Dealer and a stockholder, partner, sole proprietor, employee or affiliate that results in a diminution of the Broker Dealer's net capital shall be deemed to be an advance or loan of net capital.

Subsection III. COMPUTATION OF NET LIQUID CAPITAL (NLC)

A. General Principles.

In computing NLC, all non-allowable assets/equities, and collateralized liabilities will be deducted and allowable liabilities and equities are added to Equity per Books.

B. Computation of **Equity Eligible for Net Liquid Capital**

Equity Eligible for Net Liquid Capital shall be the sum of the following:

i. Equity as per Books;
ii. Liabilities of the Broker Dealer which are subordinated to the claims of creditors pursuant to a satisfactory subordination agreement in conformity with SRC Rule 49.1 paragraph 2 and in accordance with the following schedule:

Period remaining from RCBA Computation date to maturity date	*Allowable Inclusion*
3 years 1 day to 4 years	100%
2 years 1 day to 3 years	75%
1 year 1 day to 2 years	50%
1 year or less	0%

iii. In the case of a Broker Dealer who is a sole proprietor, the excess of liabilities which have not been incurred in the course of business as a Broker Dealer over assets not used in the business.

iv. Deposit for Futures Stock Subscription for which an application for increase in capital stock or request for exemption for registration has been filed with the Commission and the subscription, which is in the form of Allowable

Assets, shall not be withdrawn prior to SEC approval of the application/request. For net capital purposes, the same shall be considered part of aggregate indebtedness unless there is evidence that such amount is a deposit but an irrevocable subscription or a subordinated loan agreement has been entered into with the subscriber.

Provided, further, That the following items shall be excluded from Eligible Equity for Net Liquid Capital:

(1) Deferred Income Tax;
(2) Revaluation Reserves;
(3) Minority Interest and any outside investment in affiliates and associates

C. Computation of **Net Liquid Capital (NLC)**

In computing **NLC**, the Equity Eligible for Net Liquid Capital of a Broker Dealer is adjusted by the following, provided, however, that in determining net worth, all long and all short securities position shall be marked to their market value:

i. Adding unrealized profits (or deducting unrealized losses) in the accounts of the Broker Dealer.

ii. Deducting fixed assets and assets which cannot be readily converted into cash [less any indebtedness excluded in accordance with paragraph (iv) of the Definition of the term Aggregate Indebtedness] including, among other things:

a. Real estate; furniture and fixtures; Exchange memberships/trading rights; prepaid rent, insurance and other expenses; goodwill, organization expenses;

b. All unsecured advances and loans; deficits in customers' and non-customers' unsecured and partly secured notes; deficits in special omnibus accounts or similar accounts carried on behalf of another Broker Dealer, after application of calls for margin, marks to the market or other required deposits that are outstanding three (3) business days or less; deficits in customers' and non-customers' unsecured and partly secured accounts after application of calls for margin, marks to the market or other required deposits that are outstanding three (3) business days or less, except deficits in cash accounts for which not

more than one extension respecting a specified securities transaction has been requested and granted; the market value of stock loaned in excess of the value of any collateral received therefore; and any collateral deficiencies in secured demand notes in conformity with SRC Rule 49.1 (G) above.

For the purpose of the above, a loan or any other form of receivables shall be considered "unsecured" unless the following conditions exist:

(1) the receivable is secured by collateral which is otherwise unencumbered *provided, however*, that such receivable will be considered secured only to the extent of the market value of such collateral after application of such percentage deductions as may be prescribed by the Commission;
(2) the collateral is in the possession or control of the Trading Member; and
(3) the Broker Dealer has a legally enforceable written security agreement executed by the debtor in its favor under which the Trading Member shall have the power to readily sell or otherwise convert the collateral into cash.
(4) the collateral is liquid in nature and in any of the following forms:
    (a) Cash deposit in Philippine peso;
    (b) Cash deposit in foreign currency acceptable to the Commission;
    (c) Securities listed in the Exchange or other recognized stock exchanges unless specified by the Commission as not having a ready market;
    (d) Government bonds or other debt instruments which have a ready market; and
    (e) Any other collaterals which may be specified by the Commission as having a ready market;

c. Interest receivable, floor brokerage receivable, commissions receivable from other Broker Dealers, and management fees receivable from registered investment companies, all of which receivables are outstanding longer than thirty (30) days from the date they arose; dividends receivable outstanding longer than thirty (30) days from the payable date;

d. Insurance claims which, after fifteen (15) business days from the date the loss giving rise to the claim is discovered, are not covered by an opinion of an outside counsel that the claim is valid and is covered by insurance policies presently in effect; insurance claims which after thirty (30) business days from the date the loss giving rise to the claim is discovered and which are accompanied by an opinion of outside counsel described above, have not been acknowledged in writing by the insurance carrier as due and payable; and insurance claims acknowledged in writing by the carrier as due and payable outstanding longer than twenty (20) business days from the date they are so acknowledged by the carrier;

e. All other unsecured receivables; all assets doubtful of collection less any reserves established therefore; the amount by which the market value of securities failed to receive outstanding longer than thirty (30) days exceeds the contract value of such fails to receive;

f. Any receivable from an affiliate of the Broker Dealer (not otherwise deducted from net worth) and the market value of any collateral given to an affiliate (not otherwise deducted from net worth) to secure a liability over the amount of the liability of the Broker Dealer unless the books and records of the affiliate are made available for examination when requested by the Commission or the Exchange, where the Broker Dealer is a member for the Broker Dealer, in order to demonstrate the validity of the receivable or payable, or when the affiliate is an financial intermediary or entity duly registered and regulated by another government agency and that the receivable arises from an arms length transaction. The provisions of this subsection shall not apply where the affiliate is a Broker Dealer;

g. A future income tax benefit (Deferred Income Tax)

h. Any deposit with or loan to a person other than:

(1) A deposit or loan with a deposit taking institution duly authorized and registered with the Bangko Sentral ng Pilipinas (BSP);

(2) A deposit or loan to the extent the balance is secured by collateral which is Liquid, evidenced in writing and valued at

the Marked to Market value or another valued approved by the Commission;

(3) A deposit of funds as a margin to the extent that those funds relate to an open position;

i. A deposit with a third party clearing organization, unless approved by the Commission;

j. A Related Party/Associated Person Balance to the extent that the balance is not secured by collateral which is Liquid, evidenced in writing and valued at the Marked to Market value or to another value approved by the Commission;

k. A debt which was reported or created more than 30 days previously other than a debt:

(1) from another Broker Dealer that is not a Related Party or Associated Person; or
(2) which is secured by collateral which is Liquid, evidenced in writing and valued at the Marked to Market value or to another valued approved by the Commission;

l. Any prepayment which is not Liquid;

m. An Liquid Asset which has been restricted for the purpose of obtaining or creating a non-allowable or illiquid asset or set aside for use outside the ordinary course of the Broker Dealer's securities business;

n. All other assets which are not Liquid and those prescribed by the Commission as such;

iii. Deducting general guarantees and indemnities for loans and indebtedness other than those incurred by the Broker Dealer, unless otherwise permitted by the Exchange and Commission. Provided, however, that where the Broker Dealer guarantee is given to a company within the Broker Dealer's group of companies, that company's assets and liabilities (to the extent that they are covered by the Broker Dealer's guarantee) shall be taken into account as being part of the Broker Dealer's assets and liabilities for purposes of computing

NLC, and in such case the guarantee shall not be deducted from the computation unless the Exchange or Commission provides otherwise.

iv. Deducting long and short securities differences as follows:

a. Deducting the market value of all short securities differences (which shall include securities positions reflected on the securities record which are not susceptible to either count or confirmation) unresolved after discovery.

b. Deducting the market value of any long securities differences, where such securities have been sold by the Broker Dealer before they are adequately resolved, less any reserves established therefore;

c. For an Exchange member, the Exchange, and in the case of a Broker Dealer that is not a member of an Exchange, the Commission may extend the periods in paragraph C (ii)(b) above of this section for up to ten (10) business days if it finds that exceptional circumstances warrant an extension.

Subsection IV OPERATIONAL RISK

A. General Principles.

Every Broker Dealer shall always ensure that its Operational Risk Requirement is always less than its Core Equity.

B. Computation of **Operational Risk Requirement**

1. The Broker Dealer's **Operational Risk Requirement** shall be computed as:

20%	**x**	**Average of last 3 years' Gross Revenue**

2. The 3-year average gross revenue_value shall be calculated on the basis of the audited financial statements of the last three (3) years immediately preceding the date of reporting which have been filed and submitted with the Commission.

   For this purpose, the term "**Gross Revenue**" shall refer to the all sources of revenue of the Broker Dealer, net of any relevant final tax, if any, which include among, others:

   a. Commission Income
   b. Interest Revenue
   c. Net_Recovery from (provision for) market decline of marketable securities owned
   d. Rental Revenue
   d. Dividend Revenue
   e. Gain on sales of marketable securities and other assets
   f. Other gains/revenues

   For purposes of computing "**Gross Revenue**," losses are not netted against revenue accounts.

3. The Commission or the Exchange, upon prior consultation with the Commission, may include or exclude certain revenue items for purposes of determining the basis for the computation of the Operational Risk Requirement. Inclusion by the Commission of other sources of revenue in the computation of "Gross Revenue" shall not be construed as approval by the Commission for the Broker Dealer to engage in activities inconsistent with or prohibited by its secondary registration or primary franchise.

4. The Commission or the Exchange, upon prior consultation with the Commission, may require a Broker Dealer to increase its Operational Risk Requirement or set a minimum amount of operational risk requirement if the Commission or the Exchange is not satisfied that the internal control systems, corporate governance, personnel staffing, Written Supervisory Procedures and other similar processes are adequate.

Subsection V POSITION RISK

A. General Principles.

Every Broker Dealer shall compute its Position Risk Requirements for all equity, debt, and foreign exchange positions held by it as principal in accordance with the following conditions:

1. In addition to the requirements of SRC Rule 52.1, every Broker Dealer shall record separately securities held for trading purposes and those held for investment purposes. The securities in the Broker Dealer's books that are held for trading purposes shall form part of the computation of NLC and subject to position risk requirements while securities held for investment purposes shall be excluded in the computation of NLC and not subject to position risk requirements.

2. Equity securities shall be classified according to (1) Equities in PHISIX; (2) Other Equities outside the PHISIX; and (3) Equities not Listed in the Exchange but proven to be marketable, with separate position risk factors being applied to each category as provided in Schedule A;

3. Debt securities shall be classified according to (1) Republic of the Philippine Bonds; and (2) Other Corporate Debts with separate position risk factors being applied to each category as provided in Schedule A;

4. Foreign Currency positions shall likewise be subject to a position risk requirement as provided in Schedule A;

5. All debt and equity securities shall be marked to market using the closing prices of the immediately preceding trading day;

6. Where a Broker Dealer has a position in an instrument or security for which no risk treatment is provided under this section, the Broker Dealer must immediately seek clarification or guidance from the Commission's Market Regulation Department on the appropriate treatment. Pending Commission action, the Position Risk Requirement shall be one hundred percent (100%) of the marked to market value of the said instrument or security.

B. Computation of Position Risk Requirement

1. **Position Risk Requirement** shall be computed as follows:

Position Risk Requirement	=	Marked to Market value of the Instrument/Security	x	Position Risk Factor

2. Position Risk Factors

Position Risk Factors are presented in **Schedule A.**

3. Principle on Netting of long and short positions

a. Netting on long equity position against a short position is allowed provided the positions are of the same type of security.

Subsection VI Counterparty Risk Requirement

A. General Principles.

1. The Broker Dealer shall calculate its Counterparty Risk Requirement for any of the following counterparty exposures:

a. Unsettled customer trades (arising from customer-to-broker agency relationship)
b. Unsettled principal trades (arising from broker-to–broker or broker-to-Exchange/Clearing Agency relationship);
c. Loans and other dues;
d. Free deliveries;
e. Securities lending and borrowing;
f. Margin Lending;
g. Sub-underwriting arrangements or best efforts underwriting arrangements;
h. Other exposures as determined by the Exchange or Commission.

2. In the computation of the Counterparty Risk Requirement, the following rules would apply:

    a. Counterparty Risk Requirement shall be computed only for negative exposures to a counterparty and not for positive exposures.
    b. Counterparty Risk Requirement shall be calculated daily.
    c. Counterparty Exposures are marked to market.
    d. Reduction of Counterparty Risk Requirement is allowed to the extent of any of the following:
        (i) the amount of collateral that was put up to support the exposure;
        (ii) the amount of provisions made on the exposure.

    e. Offsetting of positive and negative counterparty exposures prior to calculation of Counterparty Risk Requirement is allowed provided that:
        (i) they are of the same counterparty;
        (ii) they are similar in nature in that they fall within the same class or category as enumerated in A.1 above; and
        (iii) The Broker Dealer has a valid and binding netting agreement with the counterparty.

    f. Counterparty Risk Requirement shall be computed for all counterparty exposures regardless of the relationship between the Broker Dealer and its counterparty.

3. Any other instrument which cannot be properly classified for counterweighting or is not in its standard form, shall have a Counterparty Risk Requirement for its full marked to market value, net of any collateral or discounts, until such time that the Broker Dealer obtains guidance from the Commission's Market Regulation Department on the proper treatment of such instrument or exposure.

4. The Exchange or the Commission may set a higher Counterparty Risk Requirement if, in its own judgment, the Broker Dealer may be exposed to material potential losses arising from any counterparty transaction unless the Broker Dealer can provide documentation or proof acceptable to the Exchange and Commission that its counterparty can commit to meet its obligations upon maturity. Acceptable proof may include evidence of financial standing, adequate security, or acceptable guarantees.

B. Computation of Counterparty Risk Requirement

1. **Counterparty Risk Requirement** shall be computed as follows:

Counterparty Risk Requirement (CRR)	=	**Counterparty Exposure (CE)**	x	**Counterparty Weighting (CW)**	x	**Credit Risk Factor (CRF)**

2. **Counterparty Weighting (CW)**, which is determined on the basis of the type of counterparty, is provided in **Schedule B.1.**

3. **Credit Risk Factor (CRF),** which is determined on the basis of the type or nature of counterparty exposure risk, is provided in **Schedules B.2 to B.5**. In the absence of a specific prescription as to the CRF to be applied to a particular counterparty exposure, the CRF to be used is 8%.

4. **Unsettled customer trades** (arising from customer-to-broker agency relationship)

   a. A counterparty exposure of this kind occurs when (a) the customer poses the possible risk of failing to deliver securities on a sell contract or (b) the customer poses the possible risk of failing to pay cash on a buy contract.

   b. A **negative counterparty exposure** exists when the current market value exceeds the transaction value of the stock in a sell contract. A **positive counterparty exposure** exists when the current market value is less than the transaction value of the stock in a sell contract.

   c. A **negative counterparty exposure** exists when the transaction value exceeds the current market value of the stock in a buy contract. A **positive counterparty exposure** exists when the transaction value is less than the current market value of the stock in a buy contract.

   d. Computation of the Counterparty Risk Requirement on unsettled customer trades shall be made in accordance with **Schedule B.2.**

4. **Unsettled principal trades** (arising from broker-to–broker or broker-to-Exchange/Clearing Agency relationships);

   a. A counterparty exposure risk of this kind occurs when (a) the Broker Dealer poses the possible risk of failing to receive cash from its counterparty on a sell contract or (b) the Broker Dealer poses the possible risk of failing to receive the securities from its counterparty on a buy contract.

   b. A **negative counterparty exposure** exists when the transaction value exceeds the current market value of the stock in a sell contract. A **positive counterparty exposure** exists when the transaction value is less than the current market value of the stock in a sales contract.

   c. A **negative counterparty exposure** exists when the current value exceeds the transaction value of the stock in a buy contract. A **positive counterparty exposure** exists when the current value is less than the transaction value of the stock in a buy contract.

   d. Computation of the Counterparty Risk Requirement on unsettled principal trades shall be made in accordance with **Schedule B.3.**

5. **Debts/Loans, contra losses and other amounts due**

   a. A Broker Dealer has a counterparty exposure if a debt/loan, receivable from a customer/client, contra loss, or any other amount due is not paid on its agreed due date. In the case of a contra loss, the due date shall be the date of the contra.
   b. Computation of the Counterparty Risk Requirement on debts/ loans, contra losses and other amounts due shall be made in accordance with **Schedule B.4**.

6. **Free Deliveries**

   a. A free delivery happens when the trade results from a delivery of the security or any other financial instrument to a counterparty without receiving payment or where payment is made without receiving a security or any other financial instrument.

   b. The Counterparty exposure in such cases shall be the contract value of the transaction or trade and the computation of the Counterparty

Risk Requirement on free deliveries shall be made in accordance with Subsection VI (B) above.

c. Notwithstanding the computation in Subsection VI (B) (6) (b) above, where delivery or settlement is not made within thee (3) trading days from due date, the Counterparty Risk Requirement of the Broker Dealer shall be the full contract value of the transaction.

d. For this purpose, due date shall refer to:

(1) the date of the delivery by the Broker Dealer on deliveries without receiving payment from the counterparty.
(2) The date of payment by the Broker Dealer on payments for securities without receiving securities from the counterparty.

7. **Securities Borrowing and Lending**

a. A counterparty risk exposure exists in Securities Borrowing and Lending in the following instances:

(1) For borrowing transactions, the difference between the market value of the deposit (plus accrued interest) and the value of the securities received.
(2) For lending transactions, the difference between the market value of the securities on lend (plus unpaid fees) and the value of the collateral received.

b. Computation of the Counterparty Risk Requirement on securities borrowing and lending shall be made in accordance with Subsection VI B.1 above.

8. **Margin Financing Lending**

a. For trades in Financial Instruments which are margined, the counterparty risk amount shall be:

(1) the full value of the outstanding settlement amount, premium, deposit, margin call or minimum margin maintenance that the counterparty (customer) is required to pay to the Broker Dealer, regardless of whether or not the Broker Dealer is required to pay that amount to an Exchange, clearing house or other entity;

(2) the full value of the outstanding settlement amount, premium, deposit, margin call or minimum margin maintenance that is due from an entity with respect to client or house trades cleared by that entity;

b. The counterparty risk shall commence at the time that amounts are normally scheduled for payment to the relevant exchange or clearing house.

c. A Broker Dealer may reduce the unpaid settlement amount, premium, deposit or margin call by the amount of the cash paid by the Counterparty or collateral held by the Broker Dealer on behalf of the Counterparty if the collateral is liquid, valued at the mark to market value or another value approved by the Exchange and the collateral arrangement between the Broker Dealer is evidenced in writing. The requirements of the next succeeding subsection (C) on Use of Collaterals shall apply.

d. Computation of the Counterparty Risk Requirement on Margin Financing Lending shall be made in accordance with **Schedule B.5** and Subsection VI B.1 above.

C. Use of Collateral to Reduce Counterparty Risk Exposure

1, A Broker Dealer may reduce its Counterparty Risk Exposure that serves as the basis in the computation of Counterparty Risk Requirement if sufficient collateral or security is available to cover the exposure. For purposes of determining whether the security is properly collateralized, the criteria prescribed under Subsection III (C) (ii) shall used, in so far as they are applicable.

2. The Value of the collateral used to reduce Counterparty Risk Exposure shall be net of the appropriate Position Risk Requirements as set forth in Subsection V.

3. The Commission may in the future provide additional guidelines or directives relating to the discounting of collaterals.

4. Reconciliation and inventory counts, when appropriate, should be done on all collaterals at month end.

Subsection VII Large Exposure Risk Requirement (LERR)

A. General Principles.

1. A Member Company shall compute its Large Exposure Risk Requirement in relation to -

   (i) its exposure to a single client or counterparty;
   (ii) its direct exposure to debt; and
   (iii) its direct exposure to a single equity and its group of companies;

   for all amounts arising in the normal course of trading in equity and debt securities in accordance with the provisions set out under this Subsection VII.

2. LERR shall be computed on counterparty transactions (for its exposure to a single client or counterparty) and proprietary positions (for its direct exposure to debt and single equity/issue or group of companies). For this purpose, the Counterparty Risk and Position Risk Requirements as prescribed in Subsections VI and V, respectively, shall be considered.

3. For purposes of computing the LERR for direct exposures to debt and single equity/issue or group, the position risk requirements of both securities held in proprietary accounts and as collateral of counterparties shall be aggregated.

4. The Commission may, upon written recommendation from the Exchange reduce or waive the Large Exposure Risk Requirement for specific Broker Dealers subject to terms and conditions as the Commission deems fit. The Commission may also reduce, increase, vary or waive the maximum Large Exposure Risk prescribed in this subsection as the Commission deems fit.

B. Computation of LERR

1. Exposure to a single client/counterparty

   a. A Large Exposure Risk to a single client/counterparty occurs when the total of the counterparty Risk exposure for such single client/counterparty as computed in Subsection VI (B) above exceeds ten percent (10%) of the Broker Dealer's Core Equity.

b. For purposes of computing the Broker Dealer's Large Exposure Risk in relation to a single client or counterparty, the Broker Dealer shall include its exposure to persons connected to that client or counterparty.

c. The LERR of a Broker Dealer to a single client or counterparty shall be equal to 100% of that portion of the counterparty risk exposure in excess of 10% of the Broker Dealer's Core Equity.

d. For purposes of this section, the term "single client or counterparty" includes -

(i) where such single client or counterparty is an individual, the individual, spouse of the individual, the partnership of which he is a partner, any partner of the individual, the spouse of the partner and all the companies or corporations over which the individual exercises control. For the purpose of this subsection, an individual is deemed to exercise "control" over a company or corporation if the individual or the individual's spouse, severally or jointly -

(aa) holds, directly or indirectly, more than fifty per cent (50%) of the shares of the corporation,

(bb) has the power to appoint, or cause to be appointed, a majority of the directors of the company or corporation, or

(cc) has the power to make, cause to be made, decisions in respect of the business or administration of the company or corporation, and to give effect to such decisions, or cause them to be given effect to.

(ii) where such single client or counterparty is a corporation, the corporation and its affiliated company where the company exercises management and ownership control or significant control over the corporation.

e. The maximum LERR that a Broker Dealer is allowed to carry in its books in relation to any single client or counterparty is thirty percent (30%) of its Core Equity.

f. The Broker Dealer shall report to the Exchange/Commission promptly all its Large exposure risk relating to a particular client or counterparty.

Reporting of write off of receivables of clients shall be governed by the provisions of Part IV of these Rules.

2. Direct Exposure to a debt issue

   a. A Large Exposure Risk to a single debt issue when the Large Exposure Risk in relation to an issuer of debt as computed in Subsection V (B) exceeds ten percent (10%) of the Broker Dealer's Core Equity.

   b. The LERR of a Broker Dealer to a single debt issue shall be equal to 100% of that portion of the net position or exposure in excess of 10% of the Broker Dealer's Core Equity.

   c. The maximum LERR that a Broker Dealer is allowed to carry in its books in relation to any single client or counterparty is thirty percent (30%) of its Core Equity.

   d. The Broker Dealer shall report to the Exchange/Commission promptly all its Large exposure risk relating to debt.

3. Direct exposure to a single equity relative to a particular issuer company and its group of companies;

   a. A Large Exposure Risk to a single equity relative to a particular issuer and its group of companies happens when--

      (1) LERR to Equity vs. Issuer Limit-It has a net position or exposure (either long or short) that exceeds five percent (5%) of the total listed issue of the equity; or
      (2) LERR to Equity vs. Core Equity Limit-It has a net position or exposure that exceeds ten percent (10%) of the Broker Dealer's Core Equity.

   b. For purposes of determining what constitutes net position or exposure, the Broker Dealer shall:

      (1) Include underwriting and sub-underwriting agreements which are carried as principal positions of the Broker Dealer;
      (2) Include equity OTC options or equity warrants that are in the money at its full underlying value;

(3) Not treat out of the money equity OTC options or equity warrants as an exposure;
(4) Consider as part of single equity, positions held in other listed securities of affiliates.

c. For purposes of this section, single equity relative to a particular issuer and its group of companies, shall include:

(1) Collateral underlying debtors or margin accounts (including interest);
(2) Collateral underlying loans and advances; and
(3) Investment in the stock accounts; and
(4) Other securities of a similar nature;

d. Computation of the LERR to Equity vs. Issuer limit.

(1) The Broker Dealer has to multiply the value of the exposure in excess of five percent (5%) of the total issue by the Position Risk Factor.
(2) A Broker Dealer who has an exposure of twenty percent (20%) or more of the issuer's capital shall be assumed to exercise significant influence or control over the issuer company and accordingly such investment shall not be considered part of NLC and accordingly, is not included in the computation of LERR. .

e. Computation of LERR to Equity vs. Core Equity limit

(1) A Large Exposure Risk Requirement to a single equity is computed by multiplying the value of the exposure in excess of ten percent (10%) of the Broker Dealer's Core Equity by the Position Risk Factor as described in Subsection V (A)

f. In cases where LERR to Equity is computed for both Issuer and Core Equity limits, the higher of the two values shall be chosen to represent the Broker Dealer's LERR for that particular Equity.

g. The maximum LERR that a Broker Dealer is allowed to carry in its books in relation to any equity is two hundred fifty percent (250%) of its Core Equity.

h. The Broker Dealer shall report to the Exchange/Commission promptly all its Large exposure risk relating to debt.

PART 7 EFFECTIVITY AND IMPLEMENTATION OF THE RBCA RULES

A. These Rules shall take effect fifteen (15) days after its publication in two (2) newspapers of general circulation.

B. A period of transition from the Net Capital Regime to the RBCA Regime shall commence upon effectivity of these Rules up to November 30, 2005. During such period, every Broker Dealer shall comply with the continuing reportorial requirements of the SRC and its Implementing Rules and Regulations, including the RBCA Rules.

For this purpose, every Broker Dealer is required to simultaneously submit to the Commission and the Exchange its FINOP and RBCA reports. A Statement showing a reconciliation of the differences shown in the FINOP and RBCA Reports shall likewise be submitted for efficient verification. To assist the Broker Dealer in adjusting to the new Rules during the transition period, the FINOP Report as of month-end will be submitted not later than the 15th of the succeeding month as required under the existing SRC Rules while the RBCA Report as of month-end will be submitted not later than the last day of the following month. The reconciliation report will be submitted together with the RBCA Report.

Every Broker Dealer is expected to compute its RBCA Ratio upon effectivity of these Rules. The first RBCA Report together with the reconciliation report shall be filed with the Commission and the Exchange not later than January 31, 2005 and shall reflect the computed RBCA ratio as of December 31, 2004.

The last filing of the RBCA Report together with the reconciliation report for the transition period shall be no later than the first business day of January 2006 and for the FINOP report, no later than December 15, 2005. Both reports shall reflect the computed RBCA ratio as of November 30, 2005.

Starting December 1, 2005, every Broker Dealer is expected to comply with all the requirements of the RBCA Rules. The first filing of the RBCA Report, post

transition, shall be made not later than January 16, 2006 and shall reflect the computed RBCA ratio as of December 31, 2005.

C. In filing the 2004 Audited Financial Statements, every Broker Dealer is required to submit its computations of the Adjusted Net Capital and the RBCA Ratio together with the corresponding reconciliation statement. Said computations shall be attached to and form part of the year-end Audited Financial Statements.

D. While penalties and sanctions shall not be imposed on Broker Dealers who fail to comply with the financial requirements as prescribed under Subsection II of Part 6 during the transition period, sanctions shall be imposed on Broker Dealers who fail to comply with the reportorial requirements as prescribed in these Rules or fail to show interest and effort to attain the objectives that the Commission has set during the transition period, specifically those set forth in paragraph E below.

E. During the transition period, Broker Dealers who meet the prescribed financial requirements will be encouraged to sustain compliance with the RBCA requirements while those who fail to meet the same shall be closely monitored by the Commission and the Exchange and required to submit a financial or operational plan that would allow them to comply with the RBCA requirements by December 1, 2005.

F. During the transition period, the Exchange is expected to equip its key personnel with the necessary training on the RBCA Rules, install new systems or enhance existing systems to generate timely information as required by the Rules, and develop the appropriate audit programs for the effective monitoring of Broker Dealers' compliance with the Rules.

G. Upon the effectivity of the RBCA Rules, the treatment of specific accounts shall be as follows:

1. Subordinated Loan Agreements. For purposes of applying the graduated haircut on subordinated loan agreements outstanding prior to the effectivity of the RBCA Rules, the existing requirements of SRC Rules 49.1 (1) (E) and 49.1 (2) (B) shall apply. New Subordinated Loan Agreements entered into upon effectivity of the RBCA Rules shall be covered by the requirements set forth in Part 5 (B) and Subsection III (B) of the RBCA Rules. Any renewal of existing subordinated loan agreements while the RBCA Rules are already in effect shall be

considered as new subordinated loan agreements subject to the requirements of the new Rules.

2. Investment in PSE Shares. For purposes of computing NLC, the investment in PSE Shares shall be considered as an Investment (ineligible or non-allowable asset) unless it can be proven that the PSE shares are being held for trading purposes in which case they shall be subject to the appropriate position risk requirement. However, the Commission may declare the PSE Shares as not having a ready market as defined in the Rules.

H. During the transition period, every Broker Dealer is required to formulate its own Risk Management Manual which shall be filed with the Commission for its approval on or before the deadline that will be prescribed by the Commission.

I. At the end of the transition period, SRC Rule 49.1 (1) and (2) on the Net Capital Rule and Satisfactory Subordination Agreements, respectively, shall be superseded by the relevant provisions of the RBCA Rules.

J. The Commission shall review the RBCA rules once every two (2) years. However, it may conduct a more frequent review of the Rules when it deems necessary consistent with public interest and the protection of investors.

November 11, 2004, Mandaluyong City, Philippines.

FE B. BARIN
Chairperson

FE ELOISA C. GLORIA
Commissioner

JOSELIA J. POBLADOR
Commissioner

MA. JUANITA E. CUETO
Commissioner

JESUS ENRIQUE G. MARTINEZ
Commissioner

SCHEDULE FOR PART 4
SCHEDULE FOR SPECIFIC AND GENERAL PROVISIONING FOR OVERDUE ACCOUNTS

A. Customer accounts qualifying as Non-performing Accounts

Type of account	Criteria for classification of account as non-performing	Date for classification
1. Contra losses	When the account remains unpaid starting from T + 4 or more from the date of contra transaction	T+ 4
2. Overdue purchase contracts	When the account remains unpaid starting from T + 14	T+ 14 or when the broker exercises its right of mandatory close out over the securities serving as collateral
3. Margin Accounts	When, upon making a margin call, the period to put up equity to meet the margin deficiency has expired	Upon expiration of period

B. Specific Provision

1. Specific provisions for bad and doubtful accounts shall be made for contra losses, overdue purchase contracts and margin accounts. For purposes of this section, these types of accounts are classified as Doubtful or Loss depending on the default period each respectively has. They are as follows:

Type of Accounts	Period when account is overdue	Classification
1. Contra losses	a. T+4 to 30 calendar days b. over 30 calendar days	a. **Doubtful** b. **Loss**
2. Overdue purchase contracts	a. T+14 to 30 calendar days b. over 30 calendar days	a. **Doubtful** b. **Loss**
3. Margin Accounts	When the Equity has fallen below the required minimum margin maintenance and the margin deficiency is more than P10,000.00	**Loss**

2. The Specific Provision for Doubtful accounts is computed by getting, for each doubtful account, an amount equivalent to fifty percent (50%) of the amount outstanding, net of collateral. Basis for the computation would be the individual accounts.

3. The Specific Provision for Loss Accounts is computed by getting, for each Loss account, an amount equivalent to one hundred percent (100%) of the amount outstanding, net of collateral. Basis for the computation would be the individual accounts.

4. Reversal of specific provisions is allowed under certain conditions as specified below:

Type of account	When reversal is allowed
1. Contra Losses	When full or partial payment in settlement is received to the extent that of the amount of the case received upon settlement
2. Overdue purchase contracts	When full or partial payment in settlement is received to the extent that of the amount of the case received upon settlement
3. Margin accounts	When customer's equity is increased to equal or partly meet the required initial margin or minimum margin maintenance pursuant to SRC Rule 48.1 (Margin)

5. Reversal of specific provisions is also allowed for overdue accounts initially reported by the Broker Dealer but were collected or recovered subsequent to the date of the reporting to the Commission and the Exchange but before the release of the audited financial statements of the Broker Dealers.

6. Reclassification of Non-performing account to Performing account is allowed only upon full payment or settlement of the balance (for contra losses and overdue purchase contracts) and when adequate equity is put up by the customer (for margin accounts).

C. General Provision

1. A general provision shall be established equivalent to not less than two percent (2%) of the Broker Dealer's total trade receivable net of the balance of the specific reserve for overdue accounts.
2. Total Trade Receivables refer to all collectibles from customers arising from trade conducted by the Broker Dealer inclusive of losses, commissions charges and accrued interest, whether traded via the Exchange or outside the Exchange. It excludes contracts which are not yet due for settlement.

SCHEDULE A
POSITION RISK REQUIREMENT
POSITION RISK FACTORS
SRC Rule 49 (H) Subsection V

Type of Instrument/ Security	Position Risk Factor
Equities	
Equities in the PHISIX	25%
Other Equities outside the PHISIX	35%
Other equities not listed in the Exchange and proven to be marketable	100%
Debt	
Republic of the Philippines Bonds	
• Up to 1 year	1.2%
• >1 to 5years	3.9%
• >5 to 10 years	5.3%
• >10 to 20 years	7.6%
• > 20 years	10%
Other Corporate Debts	100%
FX Position	8%

SCHEDULE B.1
COUNTERPARTY RISK REQUIREMENT
COUNTERPARTY WEIGHTING
SRC Rule 49 (H) Subsection VI

Counterparty Exposure	Weight
Government	
• National Government	0%
• Bangko Sentral ng Pilipinas (BSP)	0%
Local Government	
• Local government	20%
Financial Institutions	
• Government owned banks and financial institutions	20%
• Privately owned banks and financial institutions duly registered with the BSP	20%
• Other non-bank financial institutions duly registered with the SEC other than those affiliated with Broker Dealer	20%
• Other non-bank financial institutions duly registered with the SEC affiliated with Broker Dealer	50%
Clearing Houses and Exchanges	
• Clearing house	20%
• Registered stock and fixed income exchanges	
Registered Broker Dealers	
• Exchange Trading Participants	50%
• Non-exchange Trading Participants	50%
• Exchange /Non-Exchange Trading Participants with trading restrictions	100%
Others	100%

SCHEDULE B.2
COUNTERPARTY RISK REQUIREMENT
COUNTERPARTY RISK FACTORS FOR UNSETTLED AGENCY TRADES
SRC Rule 49 (H) Subsection VI

Agency Transaction	Time period for application of Percentage	Credit Risk Factor
1. Sell Contract - covers possible risk of failing to receive the security on a sales contract	T to T + 2 of clients	0%
	From T + 3 to T + 13 of clients	**8%** of the mark to market value of the sell contract multiplied by the CW, for negative counterparty exposure (i.e., if the current market value exceeds the transaction value of the stock) **0%** if it is a positive counterparty exposure (i.e. if the current market value is less than the transaction value of the stock)
	Beyond T + 13 of clients	The marked to market value of the contract multiplied by the CW for negative counterparty exposures (i.e., if the current market value exceeds the transaction value of the stock) **0%** if it is a positive counterparty exposure (i.e. if the current market value is less than the transaction value of the stock)
2. Buy Contract - covers possible risk of failing to give cash payment on a buy order	T to T + 2 of clients	0%
	From T + 3 to T + 13 of clients	**8%** of the mark to market value of the buy contract multiplied by the CW, for negative counterparty exposure (i.e., if the transaction value exceeds the current market value of the stock) **0%** if it is a positive counterparty exposure (i.e. if the transaction value is less than the current market value of the stock)
	Beyond T + 13 of clients	The marked to market value of the contract multiplied by the CW for negative counterparty exposures (i.e., if the transaction value exceeds the current market value of the stock) **0%** if it is a positive counterparty exposure (i.e. if the transaction value is less than the current market value of the stock)

SCHEDULE B.3
COUNTERPARTY RISK REQUIREMENT
COUNTERPARTY RISK FACTORS FOR UNSETTLED PRINCIPAL TRADES
SRC Rule 49 (H) Subsection VI

Principal Transaction	Time period for application of Percentage	Credit Risk Factor
1. Sell Contract - covers possible risk of counterparty failing to deliver securities on a sell order	T to T + 2 of counterparties (i.e. Exchange/Clearing Agency or BD)	0%
	From T + 3 to T + 13 of clients	**8%** of the mark to market value of the sell contract multiplied by the CW, for negative counterparty exposure (i.e., if the transaction value exceeds the current market value of the stock) **0%** if it is a positive counterparty exposure (i.e. if the transaction value is less than the current market value of the stock)
	Beyond T + 13 of counterparties	The marked to market value of the contract multiplied by the CW for negative counterparty exposures (i.e., if the transaction value exceeds the current market value of the stock) **0%** if it is a positive counterparty exposure (i.e. if the transaction value is less than the current market value of the stock)
2. Buy Contract - covers possible risk of counterparty failing to deliver securities on a buy contract	T to T + 2 of counterparties	0%
	From T + 3 to T + 13 of countparties	**8%** of the mark to market value of the buy contract multiplied by the CW, for negative counterparty exposure (i.e., if the current market value exceeds the transaction value of the stock) **0%** if it is a positive counterparty exposure (i.e. if the current market value is less than the transaction value of the stock)
	Beyond T + 13 of counterparties	The marked to market value of the contract multiplied by the CW for negative counterparty exposures (i.e., if the current market value exceeds the transaction value of the stock) **0%** if it is a positive counterparty exposure (i.e. if the current market value is less than the transaction value of the stock)

SCHEDULE B.4
COUNTERPARTY RISK REQUIREMENT
COUNTERPARTY RISK FACTORS FOR DEBTS/LOANS, CONTRA LOSS, AND OTHER DEBTS DUE
SRC Rule 49 (H) Subsection VI

Debt/Aging Period	Credit Risk Factor (of Counterparty Exposure)
Less than 2 days (or T+0 to T+2)	Zero
3- 13 days (or T+3 to T+13)	8% of amount due
14-30 days	50% of amount due
Over 30 days	100% of amount due

SCHEDULE B.5
COUNTERPARTY RISK REQUIREMENT
COUNTERPARTY RISK FACTORS FOR MARGIN FINANCING LENDING
SRC Rule 49 (H) Subsection VI

Credit Risk Factor (of Counterparty Exposure)
100% of net exposure