



# Bangko Sentral ng Pilipinas

## OFFICE OF THE DEPUTY GOVERNOR SUPERVISION AND EXAMINATION SECTOR

### CIRCULAR LETTER NO. CL-2010-013

To : All Banks and Non-Bank Financial Institutions

Subject : **Code of Ethics Governing Financial Market Activities in the Philippines**

Towards the end of improving financial market integrity, the Bangko Sentral ng Pilipinas (BSP) hereby informs all banks, their subsidiaries and affiliates, and other financial institutions supervised by BSP the development of "The Code of Ethics Governing Financial Market Activities in the Philippines" (Code) by the Money Market Association of the Philippines (MART). A copy of the Code is attached as Annex A for your reference.

The Code provides a set of principles and standards for market conduct of financial market participants, such as banks, brokerage firms and other financial institutions. It aims to guide market participants in determining the nature of their responsibilities to one another, clients and the market and in decision-making when faced with ethical situations. The observance of these principles and guidelines seek to promote greater professionalism in the market. The Code is anchored on the belief that high ethical standards are critical in maintaining the public's trust in the fairness of financial markets, and allowing markets to function efficiently.

The Code is generally principles-based which can be applied as a minimum standard in trading across financial product markets. The Code covers the following topics: Professionalism, Integrity of Capital Markets, Duties to Clients, Conflicts of Interest, and Duties to Market Counterparties. The BSP believes that the Code may be a basis or part of the binding market conventions governing orderly conduct / operations of the market, which is one of the components in order to recognize an over-the-counter market as an organized market.

For information and guidance.

  
NESTOR A. ESPENILLA, JR.  
Deputy Governor

24 February 2010

PANANALAPING MATATAG, BANSANG PANATAG

**Code of Ethics**  
**Governing Financial Market Activities**  
**In the Philippines**

## Table of Contents

Introduction .....	3
I. Professionalism .....	4
A. Knowledge of the Law .....	4
B. Independence and Objectivity .....	5
C. Misrepresentation .....	5
D. Misconduct .....	8
II. Integrity of Capital Markets .....	9
A. Insider Information/Material Nonpublic Information .....	9
B. Market Manipulation .....	14
III. Duties to Clients .....	15
A. Integrity, Prudence and Care .....	15
B. Fair Dealing .....	16
C. Client Suitability .....	17
D. Diligence and Reasonable Basis .....	18
E. Disclosure of Information and Communication to Clients/Public .....	19
F. Preservation of Confidentiality .....	20
IV. Conflicts of Interest .....	20
A. Disclosure of Conflicts .....	20
B. Dealing for Personal Account .....	21
C. Priority of Transactions .....	21
V. Duties to Market Counterparties .....	22
A. Knowledge of Trading Conventions .....	22
B. Firmness of Price Quotations and Deals .....	22

## INTRODUCTION

The Money Market Association of the Philippines (MART) has compiled this set of guidelines for the "Code of Ethics Governing Financial Market Activities in the Philippines" to provide a reference for banks, brokerage firms and other financial institutions in setting high ethical standards and professional excellence for market practitioners. This is anchored on the belief that high ethical standards are critical in maintaining the public's trust in the fairness of financial markets, and allowing markets to function efficiently.

The Code was designed to be generally principles-based which can be applied as a minimum standard in trading across financial product markets. It is aimed to guide members in decision-making when faced with ethical situations; and determining the nature of their responsibilities to one another, to clients and the market.

The Code of Ethics of the following associations were used to sieve the common thread of trading and selling principles: ACI Philippines, Bankers Association of the Philippines (BAP), Investment House Association of the Phils (IHAP) and MART. We also used as a reference the CFA Institute (Chartered Financial Analysts) Code of Ethics and Standards of Professional Conduct. The Appendices provide copies of the abovementioned codes used as a reference.

It is to be made clear, however, that the Code does not include trading conventions, and hence would not supercede the Trading Conventions of the different associations pertinent to their specific product markets.

It is important then that all market practitioners observe the guiding principles embodied in this Code to continue to promote greater professionalism in our treasury markets.

### NOTE:

For the purpose of the Code, the term "financial institutions" is used to represent banks, quasi-banks, thrift banks, investment houses, and brokerage firms which are members of the abovementioned associations. The term "members" is used to represent employees of the financial institutions engaged in the following banking activities, namely, money market, foreign exchange, fixed-income securities, derivatives and underwriting.

CODE OF ETHICS GOVERNING FINANCIAL MARKET ACTIVITIES  
IN THE PHILIPPINES

I. Professionalism

A. Knowledge of the Law

Financial institutions should employ the resources and procedures needed for the proper performance of its business activities. It is therefore essential that financial institutions employ or appoint persons who are qualified to conduct business with its clients and counterparties. As they are responsible for the actions and conduct of its dealers and related personnel, the financial institutions should ensure that its members have the authority, as well as the knowledge of and training on the laws governing the products and markets they are dealing with.

Members must understand and comply with all applicable laws, rules and regulations of any government, regulatory organization, or professional association governing their activities. Members must not knowingly participate nor assist in any violation of such laws, rules, or regulations.

More specifically, members should comply with the regulatory requirements issued by the Bangko Sentral ng Pilipinas (BSP) and the Securities and Exchange Commission (SEC), among others, which are relevant to the banks' trading activities in the money markets, foreign exchange, fixed income securities and derivatives, as well as in the underwriting business.

To acquire and maintain knowledge and understanding of the applicable laws, rules, and regulations, members should:

1. Stay informed. The financial institutions should establish a procedure by which members are regularly informed about the changes in the relevant laws, rules and regulations. In many instances, the banks' compliance department can provide such information in the form of memoranda distributed to the members. The members should also be abreast of current issues and developments in the products and markets they are trading. One way of keeping current is participating in in-house as well as external training courses, such as attending industry fora.

2. Review procedures. The financial institutions should review written compliance procedures on a regular basis to ensure that the procedures reflect current law and provide guidance to members what is permissible conduct under the law.
3. Maintain current files. The financial institutions should maintain readily accessible current reference copies of relevant rules and regulations.

B. Independence and Objectivity

Members must use reasonable care and judgment to achieve and maintain independence and objectivity in their professional activities. Although gifts or entertainment can be offered in the normal course of business, members must not offer, solicit, nor accept any gift, entertainment, benefit or compensation that reasonably could be expected to compromise their own independence and objectivity.

It is therefore important that the members disclose to management the gifts or benefits received. Financial institutions should establish clear policies and guidelines on when and how entertainment and gifts are to be used, supervised and monitored. At the minimum, the policies should require disclosure of details of the gifts and entertainment, with said disclosure to be submitted, preferably on a monthly basis, to the Compliance Officer and to the Board of Directors or its equivalent committee, of the member's financial institution.

The financial institution's corporate culture should fully support independence and objectivity. Given the symbiotic relationship between different business functions, say research and investment banking, one method of protecting objectivity is building a "firewall" or "Chinese wall" between these two functions. A key element of an enhanced firewall is separate reporting structures for personnel within two different business functions. This topic of "Chinese wall" will be discussed in more detail under Section II. Integrity of Capital Markets, Part A. Use of Insider Information/Material Non-Public Information.

C. Misrepresentation

A misrepresentation is any untrue statement or omission of a fact or any statement that is otherwise false or misleading.

Members must not knowingly make any misrepresentations relating to investment analysis, recommendations, actions and other professional activities. Members must not knowingly misrepresent nor give a false

impression in oral representations, advertising (whether in the press or through brochures), electronic communications, or written materials (whether publicly disseminated or not) and should not issue misleading statements about the performance of the financial institution. In this context, "knowingly" means representatives of the financial institution either know or should have known that the misrepresentation was being made.

Financial Institutions should ensure that communications with the public be done only by members with requisite authority to make public statements, or to make analysis, or provide recommendation to the general public. Communications should not contain promises of specific results, exaggerated or unwarranted claims, or unwarranted superlatives, unfounded opinions for which there is no basis or forecasts of future events which are unwarranted, or which are not clearly labeled as forecasts. Communication to the public includes disclosure or presentation of the financial institution's performance.

Members should consider several factors when determining whether communications contain misleading information such as:

1. Overall context in which the statement/s is/are made. A statement made in one context may be misleading even though such a statement could be perfectly appropriate in another context. An essential test in this regard is the balance of treatment of risks and potential benefits.
2. The audience to which the communication is directed. Different levels of explanation or detail may be necessary depending on the audience to which a communication is directed and the ability of the financial institution given the nature of the media used, to restrict the audience appropriately. If the statements made in a communication would be applicable only to a limited audience, or if additional information might be necessary for other audiences, it should be kept in mind that it is not always possible to restrict the readership of a particular communication.
3. The clarity of the communication. A statement or disclosure made in an unclear manner can result in a failure to understand the statement, or in a serious misunderstanding. A complex or overly technical explanation may cause even greater misunderstanding than too scant an information. Likewise material disclosure relegated to legends or footnotes may not generally enhance the reader's understanding of the communication.

The term communication includes, but is not limited to

1. Written material such as research reports, market letters, newspaper columns, and books.
2. Electronic communications such as Internet communications, Web pages, chat rooms, and e-mail.
3. Verbal communication such as presentations and telephone conversations.

Members must not misrepresent any aspect of its practice, including but not limited to the qualifications or credentials of its employees, the qualifications or services provided by the financial institutions, and employees' performance records as well as that of the financial institution.

In avoiding misstating or providing misleading statements, members are encouraged to fully disclose its investment performance data and must make reasonable efforts to make sure that it is fair, accurate and complete. It is important that financial institutions provide credible performance information to clients/public. If presentations made to clients are brief, the financial institution must ensure that detailed information shall be made available upon request.

In complying with the provision against misrepresentation, members should have adequate policies and procedures regarding disclosure of performance presentation and performance measurement that are consistent with regulatory requirements and the principles of fairness, accuracy and consistency. Procedures should prevent possible misrepresentations of past performance or reasonably expected performance. Historical data related to individual accounts and composite or group of accounts should be complete, fair, and accurate. In presenting past performance, the following may be considered to avoid misrepresentation:

1. Knowledge and sophistication of the audience to whom a performance presentation is addressed;
2. Including disclosures that would fully explain the performance results being reported (for example, stating, when appropriate, that results are simulated when model results are used, or disclosing whether the performance is gross of fees, net of fees, or after tax);
3. Maintaining the data and records used to calculate the performance being presented;

4. Where performance of a different type of investment product is included, stating any material difference.

Where the presentation material contains past performance information and is intended for use over a period of time, disclosures should make clear that the information may not be current and an explanation on where up-to-date past performance information may be obtained

Members must avoid spreading misinformation and rumors. Financial markets are generally responsive to news on related developments. It is not surprising therefore that gossip and misinformation emanating from various sources is often relayed through the market telephone lines and screens. These rumors can be quoted, or even originate in the financial media.

Members should not relay any information which they know to be false and should take great care when discussing unsubstantiated information, which they suspect to be inaccurate and could be damaging to a third party, be it a corporation or an individual.

#### D. Misconduct

Members must not engage in any act involving dishonesty, fraud, or deceit or commit any act that reflects adversely on their professional reputation, integrity or competence. Members must also ensure that their overall conduct and demeanor are appropriate with respect to the highest standard of professionalism as adhered to by their institution, and by the banking industry as a whole.

Professional misconduct can damage the trustworthiness or competence of an investment professional and can adversely affect a financial institution's reputation. This includes behavior that may not be illegal but could negatively affect the employee's ability to perform his or her responsibilities. For example, abusing alcohol during business hours can be considered professional misconduct because it could have a detrimental effect on the employee's ability to fulfill his or her professional responsibilities.

Members should adopt policies and procedures to prevent general misconduct:

1. Develop and/or adopt a code of ethics to which every employee must subscribe and make clear that any personal behavior that reflects poorly on the individual involved, the institution as a whole, or the investment industry will not be tolerated

2. Disseminate to all employees a list of potential violations and associated disciplinary sanctions, up to and including dismissal from the institution.
3. Check references of potential employees to ensure that they are of good character and not ineligible to work in the financial industry because of past infractions of the law.

In addition, members should have specific policies on the following:

a. Fraud

Attempts at fraud do occur and can be meticulously planned. As there are several ways in which an institution can be defrauded, great vigilance is required by management and staff, particularly so when calls are received on an ordinary telephone line (usually in principal to principal transactions).

As a preventive measure, the details of all telephone deals which do not include pre-agreed standard settlement instructions should be confirmed by email or similar means by the recipient seeking an answerback to ensure the deal is genuine.

Particular care should be taken in checking authenticity where the beneficiary is a third party or other than the transaction counterparty.

In the event of any suspicious circumstances staff must notify management without delay.

b. Gambling

Making or arranging of bets among market participants is expressly forbidden. There should be no gambling within the dealing room of a financial institution.

It is strongly recommended that management have a clearly defined written policy on the control of this activity.

c. Use of Drugs and Abused Substances

Management should take all reasonable steps to educate themselves and their staff about possible signs and effects of the use of drugs including alcohol and other abused substances. Policies should be developed and clearly announced for dealing with individuals who are found to be substances abusers, as judgment of any member dependent on such

substances may be impaired and his ability to function satisfactorily seriously diminished. A member is also likely to be vulnerable to outside inducement to conduct business not necessarily in the best interest of the firm or the market in general.

Thus, drugs and abused substances are in no way permitted inside the dealing room and, as such, users are also not allowed to enter the trading room under such influence.

## II. Integrity of Capital Markets

The orderly operation of financial markets depends greatly on the overall level of trust among all market participants. Ethical practices instill a public trust in the fairness and integrity of capital markets, enhancing their liquidity and efficiency. Financial institutions should therefore practice ethical standards that promote and maintain a high level of confidence in market integrity. The principles of transparency, disclosure, and fairness promote market integrity.

### A. Insider Information/Material Nonpublic Information

Members should not, with intent or through negligence, profit or seek to profit from insider information and material non-public information that could affect the value of an investment. Members should likewise not assist anyone with such information to make a profit for themselves, their firm or their clients.

Disclosure of material non-public information to unrelated parties and, in some cases, to related parties without consent before it becomes public is unethical and a breach of confidentiality. Dealing in financial instruments based on material non-public information about the issuer of such instruments or the instruments themselves constitutes 'insider dealing'. "Insider" is hereby defined as any individual in possession of material non-public information.

This requires that financial institutions must have in place policies and procedures to manage material non-public information. This should include, where appropriate, 'Chinese walls' to restrict the internal distribution of confidential information to those who need to know in order to be able to execute orders for customers or for compliance purposes. Material nonpublic information is not always clearly identifiable., thus, employees must be given sufficient training to either make an informed decision or consult a supervisor or compliance officer before engaging in questionable transactions.

Information is considered to be material non-public if it satisfies any of the following:

1. It has not been generally disclosed to the public and would likely affect the market price of a security or any financial instrument after being disseminated to the public and the lapse of a reasonable time for the market to absorb the information;
2. It would be considered by a reasonable person important under the circumstances in determining his course of action whether to buy, sell or hold a security or any financial instrument.

Material non-public information may include, but is not limited to, information on the following:

- Financial results of the company;
  - Mergers, acquisitions, tender offers, or joint ventures;
  - Changes in assets and/or capital structure
  - Innovative products, processes, or discoveries;
  - New licenses, patents, registered trademarks, or regulatory approval/rejection of a product;
  - Developments regarding customers or suppliers (e.g., the acquisition or loss of a contract);
  - Changes in management;
  - Change in auditor notification or the fact that the issuer may no longer rely on an auditor's report or qualified opinion;
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- Events regarding the issuer's securities (e.g., defaults on senior securities, calls of securities for redemption, repurchase plans, stock splits, changes in dividends, changes to the rights of security holders, public or private sales of additional securities, and changes in credit ratings);
  - Bankruptcies;
  - Significant legal disputes;
  - Government reports of economic trends (inflation, GDP, monetary policy, fiscal policy, currency information, etc.);
  - Issue of shares by way of public offering, rights, bonus, etc;
  - Orders for large trades before they are executed.

In addition to the substance and specificity of the information, the source or relative reliability of the information also determines materiality. The less reliable a source, the less likely the information provided would be considered material. For example, factual information from a corporate insider regarding a significant new contract for a company would likely be

material, while an assumption based on speculation by a competitor about the same contract might be less reliable and, therefore, not material.

Members must not act on and disclose insider information to make a profit for themselves, their institution or their clients. The term "insider" may include, but is not limited to, the following:

- the issuer
- a director or officer (or person performing similar functions) of, or a person controlling the issuer
- a person whose relationship or former relationship to the issuer gives or gave him access to material information about the issuer or the security that is not generally available to the public
- a government employee, or director, or officer of an exchange, clearing agency and/or self-regulatory organization who has access to material information about an issuer or a security that is not generally available to the public
- a person who learns such information by a communication from any of the foregoing insiders.

Members must be particularly aware of information that is selectively disclosed by corporations to a small group of investors, analysts, or other market participants. Information that is made available to analysts remains nonpublic until it is made available to investors in general. Corporations that disclose information on a limited basis create the potential for insider trading violations. However, under the "mosaic theory," members are free to act on the collection of material public and non-material non-public information without risking violation.

Information is "non-public" until it has been disseminated or is available to the marketplace in general (as opposed to a select group of investors). Dissemination can be defined as "made known to." For example, a company report of profits that is posted on the Internet and distributed widely through a press release or accompanied by a filing has been effectively disseminated to the marketplace.

An information barrier is the minimum procedure a financial institution should have in place to protect itself from liability. It should also consider restrictions or prohibitions on personal trading by employees and should carefully monitor both proprietary trading and personal trading by employees. It should require employees to make periodic reports (to the extent that such reporting is not already required by securities laws) of their own transactions and transactions made for the benefit of family members. Securities should be placed on a restricted list when an institution has or

may have material nonpublic information. The broad distribution of a restricted list often triggers the sort of trading the list was developed to avoid. Therefore, a watch list shown to only the few people responsible for compliance should be used to monitor transactions in specified securities. The use of a watch list in combination with a restricted list is an increasingly common means of ensuring an effective procedure.

Financial institutions should adopt policies and procedures designed to prevent the inappropriate flow of material, nonpublic information and to aid in the detection of illegal trading based on such information. An information barrier commonly referred to as a "Chinese Wall" is the most widely used approach to prevent the communication of material nonpublic information within institutions and avoid the illegal use of insider information. It restricts the flow of confidential information to those who need to know the information to perform their jobs effectively. The minimum elements of such a system include, but are not limited to, the following:

- Substantial control of relevant interdepartmental communications, preferably through a clearance area within the institution in either the compliance or legal department;
- Review of employee trading through the maintenance of "watch," "restricted," and "rumor" lists;
- Documentation of the procedures designed to limit the flow of information between departments and of the enforcement actions taken pursuant to those procedures;
- Heightened review or restriction of proprietary trading while an institution is in possession of material nonpublic information.

Any financial institution which assumes more than one function whether as dealer, broker, adviser or underwriter, or which engages in market making transactions, shall maintain proper segregation of those functions within the firm to prevent the flow of non-public material information among different parts of its organization, which perform each function. For instance, the unit/department arranging securities origination may receive inside information, i.e. the knowledge of the new issue and its likely impact on existing securities of the issuer or information provided by the issuer. Inside information gathered by the origination/deal team should not be disclosed to the other business units such as sales, trading and research.

In particular, if a member shall become aware of a potential tender offer before the tender offer has been publicly announced, such member shall not buy or sell, directly or indirectly, the securities of the target issuer until the tender offer shall have been publicly announced. Such buying or selling shall constitute insider trading.

To the extent possible, financial institutions should consider physical separation of departments and files to prevent the communication of sensitive information. For example, the investment-banking and corporate finance areas of a brokerage firm should be separated from the sales and research departments, and a bank's commercial lending department should be segregated from its trust and research departments. Other significant areas include sales, execution, research and back office settlement.

One of the primary objectives of an effective Chinese Wall procedure is to establish a reporting system in which authorized people review and approve communications between departments. The financial institution should have policies and procedures on sharing information with an end-view of maintaining the integrity of said information.

Written compliance policies and guidelines should be circulated to all employees of a financial institution. Policies and guidelines should be used in conjunction with training programs aimed at enabling employees to recognize material nonpublic information. Material nonpublic information is not always clearly identifiable. Employees must therefore be given sufficient training to either make an informed decision or consult a supervisor or compliance officer before engaging in questionable transactions.

#### B. Market Manipulation

Financial institutions must not engage in practices that distort prices or artificially inflate trading volume with the intent to mislead market participants.

This standard requires that financial institutions uphold market integrity by prohibiting market manipulation. Market manipulation includes practices that distort security prices or trading volume with the intent to deceive people or entities that rely on information in the market. Market manipulation harms the integrity of, and thereby undermines public confidence in capital markets and adversely affects interests of all investors, by disrupting the smooth functioning of the markets, distorting prices, harming the hedging functions of these markets, and creating an artificial appearance of market activity.

Market manipulation can be related to the following: