



Policy Reform Monitoring Report



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Strengthening the Enforcement and Implementation of RA 8799 or the SECURITIES REGULATION CODE

I. Executive Summary

RA 8799 or the Securities Regulation Code (SRC) was enacted in July 19, 2000 to strengthen the regulatory framework of the Philippine capital market and, in the process, help the country regain market credibility and promote portfolio investments. The SRC replaced the Revised Securities Act of 1981 (RSA), and empowered the Securities and Exchange Commission (SEC) to curtail market abuses, similar to the stock manipulation scandal involving the Best World Resources Corp. (BW) in 1999.

While the law's impact on portfolio inflows has yet to be seen, the SRC has already begun the process of reducing the level of market risk perceived by investors and of recovering market credibility. By strengthening the country's regulatory environment, investors are starting to become more confident, and have started to maintain a guarded optimism in the market's prospects.

The improvement in the country's regulatory framework brought the SEC closer to greater compliance with the "Objectives and Principles of Securities

Regulation" (OPSR) developed by the International Organization of Securities Commissions (IOSCO). Using the OPSR as benchmark, a joint World Bank/International Monetary Fund mission assessed, in December, 2001, the quality of the country's legal and regulatory framework for capital markets, and found it to be satisfactory. This assessment is supported by the Asian Development Bank's (ADB) own assessment in October of the same year.

The SRC has strengthened the SEC, thus improving market and corporate governance. It allows the Commission to make, amend, rescind or modify accounting rules to make it consistent with Internationally Accepted Standards (IAS) of accounting. It also allows the SEC to reengineer itself to better focus its attention on regulation and supervision. Finally, it gives the SEC financial independence.

RA 8799, moreover, codifies policies that strengthen Self-Regulatory Organizations (SROs) to share with the SEC the burden of regulating capital market operations. This mandate has resulted in the demutualization of the Philippine Stock Exchange

(PSE), which in August 8, 2001, converted to a stock corporation, from a non-stock organization (with mutual structure for broker-members) owned by brokers.

Feedback from some capital market players indicates that these improvements in regulation are already beginning to positively impact on the stock market. Information dissemination has improved while the activities of market jockeys (i.e. market players who try to manipulate or "jockey" the price of the stock) has been reduced.

However, although they have apparently started to mitigate the perceived market risk, these gains have yet to cause a significant improvement in portfolio inflows, whether on an absolute basis or relative to other markets in Asia.

This under-performance of the local capital market results mainly from adverse global and domestic economic, political and social factors, as well as an apparent weakness in the SEC's implementation and enforcement of the SRC. The latter is crucial because, once the exogenous factors stabilize, global funds would pour in with greater bias to more credible markets.

To further improve market credibility, the SEC should strengthen its the enforcement of the law by improving corporate governance, especially of those companies that are not listed in the PSE. It should also exact more diligence in the disclosure of companies' non-financial

information, which even for listed companies, is often hard to acquire. Moreover, it should strengthen the rights of (minority) shareholders and the role of the board of directors, and while ensuring the independence of audits.

Moreover, the SEC should oblige the PSE to fully comply with the law on demutualization. This includes the strict application of the rules on the number of non-broker members in the PSE board, on the disqualification from boards of directors of officers coming from PSE member companies, and on the PSE's ownership restrictions. Moreover, the SEC should mandate the speedier establishment of a more professional management at the PSE, in order for the latter to better implement market governance policies.

Lastly, the SEC needs to show its ability and willingness to go after the larger and more infamous SRC violators. According to some foreign brokers for example, although the SEC has successfully disrupted some financial scam operations, it appears unable to prosecute the perpetrators behind the BW scandal. In fact, some of them are even amazed that the company still trades on the PSE albeit under a different name. They had expected that the SEC should have at least put the company under suspension or imposed a penalty, which is commensurate to the damage it has caused. Negative impressions like this significantly erode RA 8799's gains with regard to strengthening the country's regulatory framework, as investors second-guess the effectiveness of regulation.

II. Background and Assessment Objective

RA 8799 or the Securities Regulation Code (SRC) was enacted in July 19, 2000 primarily to raise portfolio investments by strengthening the capital market and helping it regain its credibility. Moreover, it was passed to strengthen the SEC's regulatory powers, promote self-regulation in the securities industry, ensure protection for all investors, encourage full and fair disclosure and eliminate fraud and manipulation. The law provides for the following:

1. **Reorganization and Empowerment of the SEC.** RA 8799 allows the SEC to completely reorganize its bureaucracy and create a lean, highly skilled and professional staff, in the process establishing itself as an effective regulator of the capital markets. It gave the SEC enhanced powers to ensure a better and more efficient enforcement of the law.
2. **Codification of the full disclosure approach to regulation.** The SRC provides for the codification of the policy shift from merit-based regulation to the full disclosure approach in public offerings. The shift allows for more transparency and provides investors with more information to decide on the merits of investment options available to them. It also removes from the SEC the role of judging, for the investor, the suitability of investing in particular companies.
3. **Strengthening of market governance.** The SRC mandates the PSE to become a publicly-held corporation with diverse ownership within one year of the implementation of the law. It also provides the SEC with the power to regulate other types of trading markets, including "innovative trading" markets, to reflect new investment realities.
4. **Protection of minority shareholders.** RA 8799 requires any person or group of persons intending to acquire 15% of the equity securities of a listed or other public company, or at least 30% of such equity over a period of 12 months, to exercise mandatory tender offers to other shareholders.
5. **Prevention of market abuses.** The law contains new prohibitions against market abuses to deal with fraud. Moreover, to enable the SEC to resolve cases more expeditiously during an investigation, it provides the SEC with a flexible framework to regulate the capital markets.

After almost two years of implementation, an assessment of RA 8799's impact on the Philippine capital market and on the economy is in order. This assessment will identify whether or not the law has achieved, or is beginning to achieve, the purposes for which it was enacted, and determine possible areas in the provisions of the law, its implementing rules and regulations (IRRs) and its actual implementation that need to be refined or improved. On the part of USAID/AGILE, which was instrumental in the passage of

the new SRC and in drafting most of the implementing rules and regulations (IRRs), this assessment and analysis could identify further measures needed to push the capital market reforms initiated by RA 8799.

III. Assessment of the Impact of RA 8799

RA 8799 has improved local capital market regulation. This, according to capital market players, has already started to reduce the perceived market risk and to regain credibility for the market. The gains are more visible in terms of better information flow and the stronger legal and institutional framework.

- 1. Much improved regulatory framework.** The enactment of the SRC has improved the quality of the country's legal and regulatory framework for capital markets. This has led a joint World Bank/International Monetary Fund (WB/IMF) mission to give the country a "good housekeeping seal of approval" in December 2001. The positive review highlights the country's observance of the "Objectives and Principles of Securities Regulation" (OPSR) developed by the International Organization of Securities Commissions (IOSCO) (see Appendix 2). The IOSCO adopted the OPSR in 1998 as a yardstick with which to measure progress towards effective capital market regulation.

The OPSR principles are based on the major securities regulation objectives of

protecting investors, ensuring that markets are fair, efficient and transparent, and the reducing systemic risk. The WB/IMF observations largely agreed with some of the findings of the Asian Development Bank (ADB), which recognized that the SRC has elevated the role and power of the SEC in overseeing and regulating market activity. In fact, the enactment of the SRC prompted the ADB in end-2001, to release a vital loan package for the development of the capital markets, specifically the effort to reorganize the SEC and non-bank institutions.

The following are manifestations of the positive impact of RA 8799:

- **Reorganization.** By end of 2000, the SEC had successfully streamlined itself into a leaner organization, to better focus on capital market development and regulation. It has reduced its manpower complement by 50%, from around 555 at the head office and 60 in its seven extension offices, to a total of 278. Moreover, the SEC has complemented the reorganization process with training programs, for the reorganized workforce. Anecdotal evidence suggests that the quality of SEC employees have significantly improved as a result of this reorganization.
- **More focused operation.** The SRC has enabled the SEC to transfer some of its quasi-

judicial functions to the regional trial courts (RTCs). Between 2000 and 2001, the SEC has already delivered over a thousand cases to the RTCs, especially those involving intra-corporate disputes. This transfer of responsibilities freed up a large share the SEC's resources, the resolution of these cases taking up about half of the latter.

- **Financial independence.** RA 8799 enables the SEC to retain and utilize P100 million from its annual income. Although this amount is insufficient to finance the needs of the Commission's reorganization, it is a welcome development that signals the government's readiness to give the SEC some amount of financial independence.
- **Codification of the shift in regulatory policy to full disclosure.** The SRC codifies the policy shift, from merit-based regulation to the full disclosure approach in public offerings. This shift allows for more transparency, and provides investors with more information to decide on the merits of their investments. More importantly, it puts to rest questions on SEC interference in the market and SEC bias in matters relating to public security issuance. This gain further diminished the asymmetry of information in the capital market, to the delight of capital market players.

2. **Better corporate governance.** The enactment of RA 8799 greatly improved the Philippines' corporate governance structure as it strengthened the legal and regulatory framework set out by the Corporation Code. This observation is, in fact, manifested in the WB/IMF's favorable review of the country's standards, which is outlined in its Report on the Observance of Standards and Codes (ROSC) in September 2001. The assessment benchmarked Philippine corporate governance against the OECD Principles of Corporate Governance (OPCG) (see Appendix 3) which is recognized by the Financial Stability Forum as one of the core standards underpinning the international financial architecture. The ROSC groups the OPCG into the following major classifications: improving the disclosure of non-financial information, strengthening the rights of (minority) shareholders, enhancing the role of the board of directors, and ensuring the independence of the audit.

The following are some positive manifestations of the impact of RA 8799 on corporate governance:

- **Improving the audit.** RA 8799 has provided the SEC with the authority to improve the audit by giving it the power to make, amend, rescind or modify accounting rules to meet internationally accepted standards. Using this power, the SEC, in February 2002, approved the use of the IAS in the audit of Philippine corporations, in lieu of the

generally accepted accounting principles (GAAP). Moreover, the SEC has required external auditors to inform it of any findings of fraud or losses, in case a client-company fails to make public disclosure.

- **Codification of policies relating to SROs.** The codification of SRO- related policies removed from the SEC the task of regulating day-to-day capital market operations. This responsibility has been delegated to involved SROs, which theoretically, are in a better position to police and enforce compliance to rules affecting their members. However, although the PSE has already moved towards self-regulation, other major capital market participants have yet to register as SROs, despite the prodding of the SEC.
- **Demutualization of the PSE.** The SRC has led to the demutualization of the Philippine Stock Exchange (PSE), which on August 8, 2001, converted itself into a stock corporation, from a non-stock organization (with mutual structure for broker-members) owned by brokers. This is already a major step towards improving stock market governance, although of course, much more still needs to be done to meet the goals of demutualization.

a. *Prioritize shareholders' welfare.* The PSE still operates primarily to provide services and

minimize costs for its members, rather than for enhancing shareholders' welfare. This situation would be mitigated should the PSE adhere to the SEC's call for it to appoint an independent management, which will implement a feasible business plan.

b. *Broaden the base of ownership.* Despite the conversion of the PSE to a stock corporation, investors still confirm the existence of the "old boys club" (OBC) network in the exchange. This is because despite the PSE's mandate to open up its ownership to other investors, the PSE has yet to initiate an IPO. The PSE thus remains owned by the same members of the old PSE, which comprises the OBC network.

c. *Formulate rules and procedures on the election of the PSE board of directors (BoD).* Majority of the PSE's BoD is still made up of member-broker representatives who mostly represent smaller brokerage houses. This is in clear violation of RA 8799 which mandates that 51% of the directors should

represent non-member brokers or those who are not associated with any broker or dealer for two years prior to their election. Moreover, the SRC provides that the representation of brokers in the BoD should be based on volume/value of trade and paid up capital.

In its latest election, only seven out of 15 of the PSE's directors can be technically considered as non-member broker representatives. The PSE president, who supposedly is a non-member broker representative, headed a brokerage house a year before his election. He is thus ineligible to be a non-member broker representative (*Please refer to Table 1 below*).

This violation of the SRC is actually a repetition of a similar violation in the 2000 election, under which the president, who was initially elected in March 2000, had only then ceased to be a chairman/director of his brokerage house. Moreover, he was allowed to run for re-election the following year, and his disqualification was not even questioned. Moreover, most of the member brokers in the BoD are affiliated with smaller broker members, which again, violates the SRC.

2. Improving market credibility.

Although there is still much room for improvement, the positive impact of RA 8799 has already raised the level of the market's credibility among investors. It has improved the capital market's legal and regulatory framework and has empowered its regulatory institutions. These improvements have so far resulted in the promotion of information symmetry, which reduces insider-trading opportunities. It has curtailed the activities of market jockeys, or those market players who try to manipulate the price of the stock through illegal means.

Table 1. Representation of Members of the 2002 PSE BoD

Name	Representation
Ma. Vivian Yuchengco (Chairman)	Member
Ernest Leung (President)	Disqualified as a non-member director
Tomas Apacible	Non-member
Joaquin Bernas	Non-member
Peter Favila	Non-member
Enrique Aboitiz	Non-member
Monico Jacob	Non-member
Eugenio Lopez III	Non-member
Cayetano Paderanga	Non-member
Harry Liu	Member
Edwin Luy	Member
Federico Lim	Member
Eddie Gobing	Member
Robert Coyiuto, Jr.	Member
Alicia Rita Arroyo	Member

- **Legal framework.** RA 8799 and its implementing rules and regulations (IRRs) have adopted the best practices developed and observed in developed markets abroad. They have fortified the legal and regulatory framework set forth in the Corporation Code and allowed the country's capital market regulation to be consistent with the IOSCO principles of regulation and to approximate the OECD PCG. This early, amendments to some provisions of the SRC are already being recommended by the PSE (see appendix 1). These amendments, however, would not greatly impact on the overall credibility of the legal framework established by the SRC.

- **Institutions.** The SRC has improved the credibility of capital market institutions. Anecdotal evidence suggests that capital market players have become more comfortable with the SEC and the PSE, especially as they improve the flow of information and reduce the activities of market jockeys.

- **Information.** With the codification of the full disclosure approach to regulation, investors are now given the chance to decide on the merits of their investment, under a fuller appreciation of the risks they are taking. This has started to level the playing field in the market, as insiders lose their advantage over ordinary investors. Just

recently, this mandate has been further fortified as the PSE launched the Online Daily Disclosures Bulletin System (ODDBS). The ODDBS enables online access and viewing of circulars, memos and announcements disclosed by all listed companies during the day. These documents are converted to electronic format and entered into the system as soon as it has been prepared for release. The system is updated automatically as soon as new disclosures are entered into the system.

3. **Muted Portfolio Inflow.** Despite the various successes of RA 8799, the country has yet to generate major portfolio inflows over the past couple of years, as shown by the PHISIX, which is the barometer of the local capital market. However, the disappointing portfolio inflow cannot be entirely solved by the SRC, as exogenous factors primarily caused the problem. Nevertheless, anecdotal evidence suggests that a more credible capital market would have improved the status of the market vis a vis its peers in the region. According to capital market players, the inconsistent implementation and enforcement of the SRC mitigates the gains of the law in recapturing capital market credibility and impedes on the inflow of portfolio investments.

- **Poor absolute performance.** Despite RA 8799, the PHISIX worsened in 2001 as it fell 21.8% year-on-year. The value of trade declined by 55.4% and

market capitalization dropped by 1.5% (Please refer to Table 2 below).

Table 2. Performance of the Capital Market, 1995-2001

Year	Listed Companies	PHISIX	Market Capitalization (Billion Pesos)	Value of Trade (Billion Pesos)
1995	215	2,594.2	1,018.7	379.0
1996	216	3,170.6	1,556.8	668.9
1997	221	1,869.2	926.5	586.2
1998	222	1,968.8	967.7	408.7
1999	223	2,142.9	1,088.2	781.0
2000	230	1,494.5	746.8	357.7
2001	232	1,168.1	735.7	198.1

Source: Securities and Exchange Commission, Philippine Stock Exchange, Technistock, Inc.

This decline is largely caused by exogenous factors related to the global economic environment. In fact, international funds have been shunning Asian markets in general since the onset of the Asian crisis. This has forced equity returns, amounting to over 12.4% during the first half of the 1990's, to fall to minus 9.8% from 1995 to 2001.

- Poor relative performance.** The local capital market is not as appealing as the rest of the markets in the region. Among other things, the unstable political environment, which was highlighted during the impeachment trials of former President Estrada, has dragged down investor interest. Hence, the PHISIX ranked fourth among the worst performing indices in the region in 2001, as

per the MSCI AC FEF. The country lagged behind Malaysia, Indonesia and Thailand – the countries with which, the Philippines are normally compared with by fund managers as they have comparable market sizes (Please refer to Table 3 below).

IV. Need for better implementation and enforcement of the SRC

Although much of it could be traced to exogenous factors, the decline of the PHISIX could have been mitigated by a more significant improvement in the credibility of the market. According to market players, inconsistencies in the law's implementation and enforcement, as well as the seeming weakness of the SEC to prosecute and punish SRC offenders, erode the gains of RA 8799.

- 1. Corporate governance.** The SEC should further improve corporate governance especially of those companies, which are not listed in the PSE. The Commission

Table 3. MSCI US\$ Index of Selected Asian Countries, 1999-2001¹

	YoY % Change			Rank from worst to		
	1999	2000	2001	1999	2000	2001
Hong Kong	53.8	(18.6)	(20.3)	5.0	8.0	2.0
China	5.8	(28.8)	(25.0)	2.0	6.0	1.0
India	72.8	(19.1)	(20.3)	6.0	7.0	2.0
Indonesia	86.9	(60.4)	(14.0)	8.0	1.0	5.0
Malaysia	102.3	(12.8)	(2.2)	9.0	9.0	6.0
Philippines	(2.1)	(46.2)	(20.2)	1.0	3.0	4.0
South Korea	86.3	(44.9)	40.3	7.0	4.0	9.0
Taiwan	38.6	(42.7)	5.4	4.0	5.0	8.0
Thailand	31.3	(52.7)	1.7	3.0	2.0	7.0

Source: Securities and Exchange Commission, Philippine Stock Exchange, Technistock, Inc.

¹Data are as of 3rd week of December of each year

should exert more diligence in ensuring the disclosure of companies' non-financial information, which includes the listing of beneficial owners of companies. Moreover, it should further strengthen the rights of all shareholders, which in the past have been undermined by the inconsistent application of the tender offer rules.

2. **Market governance.** The SEC should assert its jurisdiction over the SROs and mandate the PSE to fully demutualize. Some market players and even observers are frustrated with the way the PSE has been blatantly and successfully violating the SRC, eroding the credibility of the SEC in the process. They derisively refer to an SEC "culture of exemption," under which the Commission is perceived to be subjectively applying the SRC. The perceived existence of such a culture, to them, implies weakness in enforcement.
3. **Prosecution.** The SEC should prove itself competent to implement the law, by showing that it can successfully prosecute SRC violators, especially those involved in larger cases. While it has succeeded in shutting down and disrupting the operations of 29 boiler room companies, and has issued cease-and-desist orders against 14 firms engaged in fraudulent securities transactions, investors remain unimpressed, as the SEC appears unable to prosecute the perpetrators behind the BW scandal.

V. Conclusion and Recommendation

RA 8799 was enacted when global portfolio flows were thinning out as a result of successive financial and political turmoils worldwide. Hence, even at the outset, legislators did not expect a significant inflow of funds into the country upon the law's enactment. Nevertheless, the SRC was enacted to prove to both local and foreign investors that the government is serious and has the political will to fortify the foundation of the capital market. Ultimately, it was expected that the strengthening of the capital market would make the country a less risky place for investments, and preparing it for the next upsurge in portfolio funds.

After two years of its implementation, anecdotal evidence shows that investors are beginning to accept that RA 8799 strengthened and improved the country's legal and regulatory foundation, as manifested by the demutualization of the PSE, and the improvement in market transparency. This growing acceptance, however, is still guarded as everybody agrees that a stronger foundation is necessary, but is not sufficient. The SEC still needs to consistently improve its implementation and enforcement of the law.

For example, the SEC should impose its regulatory supervision over SROs and impose its mandate over the PSE. It should avoid what market players call a "culture of exemption," by implementing the provisions of the SRC more strictly

and consistently across all market players. And most importantly, it should exhibit its ability and tenacity to punish SRC violators, especially those involved in larger and more prominent cases.

An SEC improved like so is crucial to the recovery of market credibility. Information regarding controversial matters travel through the financial industry much faster, and fund managers attach greater importance to them in making investment decisions. What better way can the SEC show its teeth, then, than by resolving the stock manipulation cases, which eroded investor confidence in the first place.

The resolution of the BW case is in fact greatly anticipated by the capital market industry, as it is a precedent to future SRC cases. An acceptable verdict would serve as a beacon to portfolio investors, while an unfavorable resolution of the case would further dampen the already battered local capital market. And a protracted hearing of the case would undermine the SEC's credibility. In fact, some players believe that the continued inaction by the SEC on the case has already given market jockeys the confidence to operate, in some post-SRC stock manipulation cases.

Appendix 1: Comments on the Proposed Amendments to RA 8800

Almost two years after its enactment, certain provisions of RA 8799 are already being recommended for amendment under, among others, House Bill (HB) 2252, as proposed by the PSE. Although it may be too early to entertain amendments at this point, it is nevertheless crucial that the points raised by HB 2253 be studied in order to ensure the smooth and sustainable rebound of the Philippine capital market. After all, the bill notes that these amendments are necessary to rectify the apparent weaknesses of RA 8799, which have allegedly stifled the growth and development of the capital market.

1. **Mandatory tender-offer rules.** Sec. 19.1 of RA 8799 mandates a person or a group of persons who intends to acquire at least 15% of any listed equity security, to make a tender offer to the rest of the shareholders of the corporation, subject to certain conditions. HB 2252 proposes to increase the threshold to 35%, in accordance with the Hong Kong Tender Offer Code.

The acceptance of this amendment would undermine the spirit of the tender offer rule. Considering that, the average free float in the Philippine stock market ranges between 30% to 40%, the amendment would make the provision almost inoperable. This is more glaring if we consider that smaller companies, which are generally almost family-owned, have a free float of between 10% to 15%. Hence, by raising the tender offer limit to 35%, minority shareholders rights would be further weakened, to the prejudice of corporate governance.

Free float refers to the amount of shares in the market, which are not committed to any entity, and which are freely traded everyday. Although this should theoretically equal the number of shares listed in the exchange, in most cases, certain entities would buy a significant number of shares either for accounting or control purposes. In these cases, the shares would then be taken out of the free float computation, as they would indefinitely not be available for sale.

2. **Broker-director/dealer prohibition.** HB 2252 hopes to liberalize the application of the broker-director prohibition, by allowing the SRO, rather than the regulator, to implement the rule based on its reading of the needs of the market during the time. The proposed amendments hope to repeal Sec. 34.1 of RA 8799, which imposes a broker-dealer prohibition.

While the Philippine capital market is still in its infancy, these proposed amendments seem more logical. The original provisions of the law seem to overlook the inevitability of overlapping functions in the Philippine capital market and is thus, seen as too limiting for a small emerging market.

3. **Minimum capital requirement.** Sec.28.4 of the SRC has given the SEC authority to promulgate rules pertaining to the minimum net capital requirement of brokers and dealers. The proposed amendment to RA 8799 hopes to transfer the authority to mandate these capitalization requirements to the respective SRO, and to allow the SRO to implement other fitting capital adequacy requirements.

This proposed amendment is consistent with the logic behind converting capital market organizations into SROs. Approving this amendment at this time, could however be counter productive, because until the PSE is fully deregulated, the old boys club network could effectively lobby for the easing of the capital adequacy requirements, which would greatly undermine the stability of the PSE. Such stability is essential in the government's effort in regaining market credibility.

4. **Limitation on ownership and representation of brokers in an exchange.** Sec. 33.2 (c) of the SRC prohibits a single person, entity, or aligned individuals or entities from

controlling the exchange. However, the prohibition of the law encompasses even those individuals who belong to the same industry or business group (e.g. members of the same Chamber of Commerce and Industry groups or other similar business clubs). HB 2252 hopes to amend the law by taking the latter prohibition out.

The amendatory bill hopes to repeal Sec. 33.2 (f) of the SRC, which provides for the representation of brokers in the board of the exchange based on volume/value of trade and paid up capital. The PSE believes that this rule is contrary to the provisions of the corporation code, which bases the power of the shareholders on their number of shares. This amendment is seen as dangerous if approved, as it would nearly codify the existence of the old boys club network. In as much as the demutualization of the exchange equally divided the available shares of the PSE to the old brokers, the latter would naturally control the corporation.

Appendix 2: Categories of and the IOSCO Principles of Securities Regulation

Categories	IOSCO principle nos.
Relating to the regulator	1 to 5
Self-regulation	6 to 7
Enforcement of securities regulation	8 to 10
Cooperation in regulation	11 to 13
For issuers	14 to 16
Collective investment schemes	17 to 20
Market intermediaries	21 to 24
Secondary market	25 to 30

Number	Principle
1	The responsibilities of the regulator should be clear and objectively stated
2	The regulator should be operationally independent and accountable in the exercise of its function and powers
3	The regulator should have adequate powers, proper resources and the capacity to perform its functions and exercise its powers
4	The regulator should adopt clear and consistent regulatory processes
5	The staff of the regulator should observe the highest professional standards including appropriate standards of confidentiality
6	The regulatory regime should make appropriate use of SROs that exercise some direct oversight responsibility for their respective areas of competence, and to the extent appropriate to the size and complexity of the markets
7	SROs should be subject to the oversight of the regulator and should observe standards of fairness and confidentiality when exercising powers and delegated responsibility
8	The regulator should have comprehensive inspection, investigation and surveillance powers
9	The regulator should have comprehensive enforcement powers
10	The regulatory system should ensure an effective and credible use of inspection, investigation, surveillance and enforcement powers and implementation of an effective compliance program
11	The regulator should have authority to share both public and non-public information with domestic and foreign counterparts
12	Regulators should establish information sharing mechanisms that set out when and how they will share both public and non-public information with their domestic and foreign counterparts
13	The regulatory system should allow for assistance to be provided to foreign regulators who need to make inquiries in the discharge of their functions and exercise of their powers
14	There should be full, accurate and timely disclosure of financial results and other information that is material to investors' decisions
15	Holders of securities in a company should be treated in a fair and equitable manner
16	Accounting and auditing standards should be of a high and internationally acceptable quality
17	The regulatory system should set standards for the eligibility and the regulation of those who wish to market or operate a collective investment scheme
18	The regulatory system should provide for rules governing the legal form and structure of collective investment schemes and the segregation and protection of client assets
19	Regulation should require disclosure, as set forth under the principles of issuers, which is necessary to evaluate the suitability of a collective investment scheme for a particular investor and the value of the investors' interest in the scheme
20	Regulation should ensure that there is a proper and disclosed basis for asset valuation and the pricing and the redemption of units in a collective investment scheme
21	Regulation should provide for minimum entry standards for market intermediaries
22	There should be initial and ongoing capital and other prudential requirements for market intermediaries that reflect the risks that the intermediaries undertake

23	Market intermediaries should be required to comply with standards for international organization and operational conduct that aim to protect the interests of clients, ensure proper management of risk, and under which management of the intermediary accepts primary responsibility for these matters
24	There should be a procedure for dealing with the failure of a market intermediary in order to minimize damage and loss to investors and to contain systemic risk
25	The establishment of trading systems including securities exchanges should be subject to regulatory authorization and oversight
26	There should be ongoing regulatory supervision of exchanges and trading systems, which should aim to ensure that the integrity of trading is maintained through fair and equitable rules that strike an appropriate balance between the demands of different market participants
27	Regulation should promote transparency in trading
28	Regulation should be designed to detect and deter manipulation and other unfair trading practices
29	Regulation should aim to ensure the proper management of large exposures, default risk and market disruption
30	Systems for clearing and settlement of securities transactions should be subject to regulatory oversight, and designed to ensure that they are fair, effective and they reduce systemic risk

Appendix 3: OECD Principles of Corporate Governance

Section	Principle
I	Rights of shareholders
	The corporate governance framework should protect shareholders' rights. Basic shareholder rights include the right to: <ul style="list-style-type: none"> • Secure methods of ownership registration • Convey or transfer shares • Obtain timely and regular relevant information on the corporation • Participate and vote in general shareholder meetings • Elect members of the (supervisory) board • Share in the profits of the corporation
	Shareholders have the right to participate in, and to be sufficiently informed on, decisions concerning fundamental corporate changes, such as: <ul style="list-style-type: none"> • Amendments to the governing documents of the company • The authorization of additional shares • Extraordinary transactions that in effect result in the sale of the company
	Shareholders should have the opportunity to participate effectively and vote in general shareholder meetings and should be informed of the rules, including voting procedures that govern general shareholder meetings.
	Capital structures and arrangements that enable shareholders to obtain a degree of control disproportionate to their equity ownership should be disclosed.
	Markets for corporate control should be allowed to function in an efficient and transparent manner.
	Shareholders, including institutional investors, should consider the costs and benefits of exercising their voting rights.
II	Equitable treatment of shareholders
	The corporate governance framework should ensure the equitable treatment of all shareholders, including minority and foreign shareholders. All shareholders should have the opportunity to obtain effective redress for violation of their rights. All shareholders of the same class should be treated equally.
	Insider trading and abusive self-dealing should be prohibited.
	Members of the board and managers should be required to disclose any material interests in transactions, or matters affecting the corporation.
III	Role of Stakeholders in Corporate Governance
	The corporate governance framework should recognize the rights of other stakeholders (i.e. employees and creditors) as established by law and encourage active co-operation between corporations and stakeholders in creating wealth, jobs, and the sustainability of financially sound enterprises. The corporate governance framework should assure that the rights of stakeholders that are protected by law are respected
	Where stakeholder interests are protected by law, stakeholders should have the opportunity to obtain effective redress for violation of their rights
	The corporate governance framework should permit performance-enhancement mechanisms for stakeholder participation
	Where stakeholders participate in the corporate governance process, they should have access to relevant information.
IV	Disclosure and Transparency
	The corporate governance framework should ensure that timely and accurate disclosure is made on all material matters regarding the corporation, including the financial situation, performance, ownership, and the governance of the company. Disclosure should include but not be limited to, material information on the following sections: <ul style="list-style-type: none"> • Financial and operating results • Company objectives

Section	Principle
	<ul style="list-style-type: none"> • Major share ownership and voting rights • Board members, key executives and their remuneration • Material foreseeable risk factors • Material issues regarding employees and other stakeholders • Governance structures and policies
	Information should be prepared, audited, and disclosed in accordance with high quality standards of accounting, financial and non-financial disclosure, and audit
	An annual audit should be conducted by an independent auditor in order to provide an external and objective assurance on the way in which financial statements have been prepared and presented
	Channels for disseminating information should provide for fair, timely and cost-effective access to relevant information by users
V	Responsibilities of the Board
	The corporate governance framework should ensure the strategic guidance of the company, the effective monitoring of management by the board, and the board's accountability to the company and the shareholders. Board members should act on a fully informed basis, in good faith, with due diligence and care, and in the best interest of the company and the shareholders
	Where board decisions may affect different shareholder groups differently, the board should treat all shareholders fairly
	The board should ensure compliance with applicable law and take into account the interests of stakeholders
	<p>The board should fulfill certain key functions, including the following:</p> <ul style="list-style-type: none"> • Corporate strategy, risk policy, budgets, business plans, performance objectives, implementation and performance surveillance, major capital expenditures, acquisitions, divestitures • Selection, monitoring, replacement of key management • Key executive and (supervisory) board remuneration, (supervisory) board nomination • Monitoring of conflict of interest of management, (supervisory) board members, and shareholders, including misuse of corporate assets and abuse in related party transactions. • Ensuring integrity of accounting and financial reporting systems, including independent audit, systems of control, compliance with law • Monitoring governance practices and making necessary changes • Overseeing disclosure and communication
	The board should be able to exercise objective judgment on corporate affairs independent, in particular, from management
	In order to fulfill their responsibilities, board members should have access to accurate, relevant and timely information

Appendix 4: WB/IMF Policy Recommendation on Corporate Governance

The WB/IMF came out with their ROSC in September 2001, which benchmarked Philippine corporate governance against the OECD Principles of Corporate Governance. The policy recommendations in this ROSC highlighted areas where the Philippine corporate governance system could be strengthened. These recommendations are grouped under four main headings: improving the disclosure of non-financial information, strengthening the rights of (minority) shareholders, enhancing the role of the board of directors, and ensuring the independence of the audit.

The report also noted that, throughout the corporate governance regime in the Philippines, enforcement requires strengthening. A number of the areas where enforcement needs to be enhanced, including the sanctioning powers of the SEC and the PSE, are being addressed in collaboration with the Asian Development Bank.

1. Disclosure of non-financial information

- Ensure a mechanism for both the regulators and shareholders to identify the component parts of the capital structure and the beneficial ownership of holdings in excess of an agreed margin (five percent)
- To promote improved transparency, make the register of beneficial owners publicly available, via internet and for one site inspection by the SEC

2. The rights of (minority) shareholders

- Empower minority shareholders to play a more effective role in corporate governance by introducing a provision to allow shareholders to convene directly a meeting of the company, without having to petition the regulator, and for the company to circulate the agenda
- Introduce a provision to allow shareholders to put forward proposals to the agenda, or counterproposals to management agendas and ensure these are practical for minority shareholders regarding cost, timetable and information.
- Review provisions governing duties of the majority in relation to the minority, and consider limiting voting rights on matters where the majority has a conflict of interest
- Review the minimum free float for listed companies, ensuring it corresponds with the special voting protections for minority shareholders (such as the qualified majority provisions of two-thirds, which would only be effective with a greater than one third holding by minorities)
- Consider introducing a provision for voting by mail.
- Consider the establishment of an association or institution to protect the interests of minority shareholders, which could provide independent advice, research and voting services.
- Consider the introduction of a requirement for fiduciary investors, such as pension funds, to disclose their policies on corporate governance, to exercise their voting rights in the sole interests of the beneficiaries.

3. The role of the board of directors

- Strengthen the mechanisms by which the board of directors governs the affairs of the company as mandated by law.
- Strengthen provisions governing self-dealing and conflicts of interest for directors
- Review disclosure provisions for directors to ensure they allow shareholders to fully assess independence to include all relevant information, particularly in relation to previous corporate directorships .

- Require disclosure of board practices on corporate governance benchmarked against a Philippine code of best practice which reflects international norms (including the establishment of independent audit committees, statements on internal control and going concern, disclosure of attendance at board meetings, nomination and review of performance, and stakeholder relations).
- Consider the introduction of training requirements for directors, and continuing professional education, with disclosure of training undertaken, particularly to ensure a full understanding of legal duties and liabilities.
- Introduce a requirement for directors to review and sign off on the auditor's long form report.

4. The independence of the audit

- Require disclosure of all personal or business relationships, past or current, between the audit firm, its partners, the company, its directors and all related parties
- Require disclosure of full audit and non-audit fees paid to the audit firm by the company and its related parties
- Review general provisions regarding independence, including rotation of audit partner or firms
- Require the establishment of audit committees composed of a majority of independent directors, with responsibility for both internal and external audit
- Require training for members of audit committees to ensure financial numeracy