

## 136 RELATED PARTY TRANSACTIONS

**Policy statement.** The Bangko Sentral recognizes that transactions between and among related parties create financial, commercial and economic benefits to individual institutions and to the entire group where said institutions belong. In this regard, related party transactions are generally allowed: *Provided*, That these are done on an arm’s length basis. The Bangko Sentral expects banks, including their non-bank financial subsidiaries and affiliates, to exercise appropriate oversight and implement effective control systems for managing said exposures as these may potentially lead to abuses that are disadvantageous to the bank and its depositors, creditors, fiduciary clients, and other stakeholders.

### **RPT policies/roles of senior management and self-assessment functions.**

a. The RPT policies shall include, but not be limited to the following:

- (1) *Definition of related parties.* The policy shall clearly define “related parties”. It shall identify persons and companies that are considered the BSFI’s related parties. The policy shall require management to periodically review and update the inventory of related parties to capture organizational and structural changes in the BSFI and its related parties.
- (2) *Coverage of RPT policy.* The coverage of the RPT policy shall capture a broader spectrum of transactions, covering not only those that give rise to credit and/or counterparty risks but also those that could pose material/special risk or potential abuse to the BSFI and its stakeholders.

Transactions that were entered into with an unrelated party that subsequently becomes a related party may be excluded from the limits and approval process required in the policy. However, any alteration to the terms and conditions, or increase in exposure level, related to these transactions after the non-related party becomes a related party shall subject the RPT to the requirements of the policy. The prospective treatment should, however, be without prejudice to supervisory actions that may be enforced for transactions noted to have not been conducted on an arm’s length basis.

- (3) *Guidelines in ensuring arm’s length terms.* The policy shall have clear guidelines in ensuring that RPTs are conducted in the regular course of business and not undertaken on more favorable economic terms (e.g., price, commissions, interest rates, fees, tenor, collateral requirement) to such related parties than similar transactions with non-related parties under similar circumstances. This shall include guidance for an effective price discovery mechanism to ensure that transactions are engaged into at terms that promote the best interest of the BSFI and its stakeholders. The price discovery mechanism may include, but not limited to,

acquiring the services of an external expert, opening the transaction to a bidding process, or publication of available property for sale.

- (4) *Conflicts of interest.* The policy shall cover the identification and prevention or management of potential or actual conflicts of interest which may arise. The members of the board of directors, stockholders, and management shall disclose to the board of directors whether they directly, indirectly or on behalf of third parties, have a financial interest in any transaction or matter affecting the BSFI. Directors and officers with personal interest in the transaction shall abstain from the discussion, approval and management of such transaction or matter affecting the BSFI.
- (5) *Materiality thresholds and excluded transactions.* The policy shall include materiality thresholds for RPTs, which shall be set at a level where omission or misstatement of the transaction could pose significant risk to the BSFI and could influence the economic decisions of its board of directors.

Materiality threshold may be set for each type of transaction and for each related party group, depending on the nature of the transaction and risks involved. The RPT policy may also identify transactions excluded from the materiality threshold requirement, such as transactions concerning deposit operations, regular trade transactions involving purchases and sales of debt securities traded in an active market, and those granted under Bangko Sentral approved fringe benefit programs. Materiality threshold levels will vary from one BSFI to another depending on the nature, scope, frequency, value of, and risks associated with the RPT. The BSFI shall document the justifications for the materiality thresholds and exclusions set.

The Bangko Sentral may direct a BSFI to reduce its materiality threshold or amend excluded transactions if the Bangko Sentral deems that the threshold or exclusion is inappropriate considering the BSFI's size, risk profile, and risk management systems.

- (6) *Internal limits for individual and aggregate exposures.* To ensure that RPTs are within prudent levels, the policy shall, in addition to existing prudential limits which shall be complied with at all times, include internal limits or sub-limits for individual and aggregate exposures to a related party and for aggregate exposures to all related parties that are consistent with the BSFI's risk appetite, risk profile, and capital strength.

The internally-set limits shall be tied in with the BSFI's internal definition of capital. Breaches in limits shall be reported to the board of directors with the decision of the board of directors to accept the exposure or to take steps to address the breaches, as may be

necessary, duly documented in the minutes of meetings.

- (7) *Whistleblowing mechanisms.* The policy shall include effective whistleblowing mechanisms consistent with the corporate values and codes of conduct set by the board of directors. The policy shall encourage employees to communicate, confidentially and without the risk of reprisal, legitimate concerns about illegal, unethical or questionable RPTs. It shall include guidance on how and by whom legitimate material concerns should be reported, investigated and addressed by an objective independent internal or external body, senior management and/or the board of directors itself.
- (8) *Restitution of losses and other remedies for abusive RPTs.* The policy shall include measures that would cut losses and allow recovery of losses or opportunity costs incurred by the BSFI arising from RPTs that are not engaged on arm's length terms. The policy shall also include the manner of handling personnel, officers or directors, who have been remiss in their duties in handling RPTs.

The overarching policy will consolidate all existing policies that address the above requirements or may make reference to already existing policies.

- b. *Roles of senior management and self-assessment functions.* Senior management shall implement appropriate controls to effectively manage and monitor RPTs on a per transaction and aggregate basis. Exposures to related parties shall also be monitored on an ongoing basis to ensure compliance with the BSFI's policy and Bangko Sentral's regulations.

The internal audit function shall conduct a periodic formal review of the effectiveness of the BSFI's system and internal controls governing RPTs to assess consistency with the board-approved policies and procedures. The resulting audit reports, including exceptions or breaches in limits, shall be communicated directly to the audit committee.

The compliance function shall ensure that the BSFI complies with relevant rules and regulations and is informed of regulatory developments in areas affecting related parties. It shall aid in the review of the BSFI's transactions and identify any potential RPT that would require review by the Board or RPT Committee. It shall ensure that the RPT policy is kept updated and is properly implemented throughout the BSFI.

**Disclosure and regulatory reporting.** Banks shall adequately disclose in their Annual Report, if applicable, the overarching policies and procedures for managing RPTs, including managing of conflicts of interest or potential conflicts of interest; responsibility of RPT Committee; nature, terms and conditions, as well as original and outstanding individual and aggregate balances, including off-balance

sheet commitments, of material RPTs.

In addition to the required reports on DOSRI and transactions with subsidiaries and affiliates under existing regulations:

- a. UBs/KBs that are part of conglomerates shall report all entities in the conglomerate structure where it belongs. The conglomerate structure shall likewise disclose beneficial owners of shareholdings that are in the name of PCD Nominee Corporation. The report on conglomerate structure shall be submitted to the Bangko Sentral within thirty (30) calendar days after the end of every calendar year.
- b. Banks shall submit a report on material exposures to related parties, which shall include the material RPTs of their non-bank financial subsidiaries and affiliates, based on the bank's internal definition within twenty (20) calendar days after the end of the reference quarter starting with the quarter ending 31 March 2016. Supervised non-bank financial subsidiaries and affiliates are therefore expected to report their material RPTs to the parent bank, which in turn shall report same to the Bangko Sentral.

Transactions concerning deposit operations, credit card availments, regular trade transactions involving purchases and sales of debt securities traded in an active market, are excluded from the reporting requirement to Bangko Sentral: *Provided*, That credit card lines with amounts falling within the definition of "material transactions" shall be reported to the Bangko Sentral upon approval of the line.

Lease contracts and other similar contracts with recurring payment transaction shall only be reported once, upon approval of said transaction by the board of directors. In case the parties involved in the transactions are both supervised by the Bangko Sentral, only the lessor, in case of a lease contract, or the party engaging/requesting for the services of the other bank, in case of other contracts, shall submit the report.

This section amends the reporting requirement on group structure and the report on significant transactions required under Item "d(8)" of Sec. 132 (*Specific duties and responsibilities of the board of directors*).

**Applicability to branches of foreign banks.** The governance principles and requirements embodied in this Section shall be complied with by branches of foreign banks, to the extent possible, given their distinct organizational set-up. The General Manager or Country Manager is the principal officer that will oversee the implementation of the governance principles embodied in this Section. Branches of foreign banks are not covered by the reportorial requirement on conglomerate structure.

**Supervisory enforcement actions.** The Bangko Sentral reserves the right to deploy its range of supervisory tools to promote adherence to the requirements set forth in the guidelines under this Section and bring about timely corrective actions and compliance with Bangko Sentral directives. The Bangko Sentral considers abuses in credit to related parties as serious offenses and shall be dealt with severely. In this regard, abuse shall be interpreted to include extending credit to related parties without adopting appropriate internal policies. For this purpose, the Bangko Sentral may, among others, issue directives or sanctions on the bank and responsible persons, which may include restrictions or prohibitions of lending to related parties or from certain authorities/activities, restrictions or prohibitions on dividend declarations; and warning, reprimand, suspension, removal and disqualification of bank directors, officers and/or employees concerned.

*(Circular Nos. 969 dated 22 August 2017, 917 dated 08 July 2016, 914 dated 23 June 2016, and 895 dated 14 December 2015)*