



Republic of the Philippines
Department of Finance
INSURANCE COMMISSION
1071 United Nations Avenue
Manila



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CIRCULAR LETTER

TO : ALL INSURANCE/REINSURANCE COMPANIES, MUTUAL BENEFIT ASSOCIATIONS (MBAs), PRE-NEED (PN) COMPANIES AND HEALTH MAINTENANCE ORGANIZATIONS (HMOs) AUTHORIZED TO TRANSACT BUSINESS IN THE PHILIPPINES

SUBJECT : Guidelines on Related Party Transactions for Insurance Commission's (IC) Covered Institutions (CIs)¹

The Insurance Commission recognizes the importance of establishing and maintaining policies and procedures for transactions between related parties. These policies shall be made to ensure that such transactions are only undertaken on an arm's length basis for the financial, commercial and economic benefit of the given CI and the entire group where the said institution belongs. The IC expects every single CI including its 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 CI and its policyholders, members, planholders, card holders, claimants, creditors, fiduciary clients, and other stakeholders.

1. For purposes of this Circular, the following definitions shall apply:

1.1 Related parties² shall cover the IC-CIs' subsidiaries as well as affiliates and special purpose entities that the CI exerts direct/indirect control over or that exerts significant influence³ over the CI; the directors; officers; stockholders and related interests and their close family members, as well as corresponding persons in affiliated companies. This shall also include such other person/juridical entity whose interests may pose potential conflict with the interest of the CI, hence, is identified as a related party.

- 1 Covered institutions (CI) shall include insurance and reinsurance companies, Mutual Benefit Associations (MBAs), Pre-Need (PN) companies and Health Maintenance Organizations (HMOs) and their intermediaries
- 2 Under PAS 24 – Related parties include the parents, entities with joint control or significant influence over the entity, subsidiaries, associates, joint ventures in which the entity is a venture, key management personnel of the entity or its parent; and other related parties.
- 3 Under PAS 24 – Significant Influence is the power to participate in the operating and financial policy decisions of an entity; it is not control over those policies. It may stem from share ownership, statute or agreement and may be exercised by representation on the board of directors, participation in the policy-making process, material inter-company transactions, interchange of management personnel and dependence on technical information

- 1.2 **Close family members** are persons related to the CI's directors, officers and stockholders (DOS) within the second degree of consanguinity or affinity, legitimate or common-law. These shall include the spouse, parent, child, brother, sister, grandparent, grandchild, parent-in-law, son-/daughter-in-law, brother-/sister-in-law, grandparent-in-law, and grandchild-in-law of the CI's DOS.
- 1.3 **Corresponding persons in affiliated companies** are the DOS of the affiliated companies and their close family members.
- 1.4 **Under Section 290 of the Insurance Code**, as amended by R.A. 10607: Control is presumed to exist if any person directly or indirectly owns, controls or holds with the power to vote forty percent (40%) or more of the voting securities of any other person. Provided, That no person shall be deemed to control another person solely by reason of his being an officer or director of such other person.
- 1.5 **Control of an enterprise** exists when there is:
 - 1.5.1 Under Section 4 (i) of the Pre-Need Code: Affiliate of, or affiliated with, a specified person refers to a person that directly or indirectly, through one (1) or more intermediaries, controls, or is controlled by, or is under common control with, the person specified. Exercising control over a legal entity shall mean any one of the following: (1) owning either solely or together with affiliated persons more than twenty-five percent (25%) of the outstanding capital stock of a legal entity; and (2) being an officer or director of such legal entity.
 - 1.5.2 Power to govern the financial and operating policies of the enterprise under a statute or an agreement; or
 - 1.5.3 Power to appoint or remove the majority of the members of the board of directors or equivalent governing body; or
 - 1.5.4 Power to cast the majority votes at meetings of the board of directors or equivalent governing body; or
 - 1.5.5 Any other arrangement similar to any of the above.

Should the CI choose to disclaim or rebut the presumption, it should provide facts sufficient to show that there is indeed no control. Further, the CI shall submit a written commitment that : (1) shares owned or held are exclusively for investment purposes; (2) the CI-stockholder will not serve on the board of directors and will not nominate any candidate to serve on

the board or otherwise seek board representation; (3) the CI-stockholder will have only limited contacts with the management that are customary for interested shareholders; (4) the CI-stockholder will engage only in normal and customary transactions with the enterprise; and (5) the CI will not pledge the shares acquired to secure a loan with any institution.

1.6 Related party transactions are transactions or dealings with related parties of the CI, including its trust department, regardless of whether or not a price is charged. These shall include, but not limited to the following:

- 1.6.1 On-and off-balance sheet credit exposures and claims and write-offs;
- 1.6.2 Investments and/or subscriptions for debt/equity issuances;
- 1.6.3 Consulting, professional, agency and other service arrangements/contracts;
- 1.6.4 Purchases and sales of assets, including transfer of technology and intangible items (e.g. research and development, trademarks and license agreements);
- 1.6.5 Construction arrangements/contracts;
- 1.6.6 Lease arrangements/contracts;
- 1.6.7 Trading and derivative transactions;
- 1.6.8 Borrowings, commitments, fund transfers and guarantees;
- 1.6.9 Sale, purchase or supply of any goods or materials; and
- 1.6.10 Establishment of joint venture entities

RPTs shall be interpreted broadly to include not only transactions that are entered into with related parties but also outstanding transactions that were entered into with an unrelated party that subsequently becomes a related party.

1.7 Insurance group⁴ refers to a group structure which contains two or more insurers

2. Duties and Responsibilities/Roles and Functions of the CI's Board of Directors

2.1 The board of directors shall have the overall responsibility in ensuring that transactions with related parties are handled in a sound and prudent manner, with integrity, and in compliance with applicable laws and regulations to protect the interest of policyholders, members, planholders, card holders, claimants, creditors and other stakeholders. Towards this end, the Board of Directors shall carry out the following duties and responsibilities:

⁴ Principles Applicable to the Supervision of International Insurers and Insurance Groups and their Cross Border Business Operations issued by IAIS Technical Committee approved on December 8, 1999.

- 2.1.1 To observe good governance and approve an overarching policy on the handling of RPTs to ensure that there is effective compliance with existing laws, rules and regulations at all times, that these are conducted on an arm's length basis, and that no stakeholder is unduly disadvantaged. A group-wide RPT policy shall be adopted, encompassing all entries within the group, taking into account their size, structure, risk profile and complexity of operations.

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

- a. *Definition of related parties.* The policy shall clearly define "related parties". It shall identify persons and companies that are considered the CI'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 CI and its related parties.
- b. *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 CI and its stakeholders.
- c. *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 CI 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.
- d. *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, stockholders, and management shall disclose to the board whether they directly, indirectly or on behalf of third parties, have a financial interest in any transaction or matter affecting the CI. Directors and officers with personal interest in the transaction shall abstain from the discussion,

approval and management of such transaction or matter affecting the CI.

- e. *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 CI 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 regular trade transactions involving purchase and sales of debt securities traded in an active market.

Materiality threshold levels will vary from one CI to another depending on the nature, scope, frequency, value of, and risks associated with the RPT. The CI shall document the justifications for the materiality thresholds and exclusion set.

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

- f. *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 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 CI's risk appetite, risk profile and capital strength.

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

- g. *Whistle blowing 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 itself.

- h. *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 CI arising from RPTs that are not engaged or 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.

- 2.1.2 To approve all material RPTs, those that cross the materiality threshold, and write-off of material exposures to related parties, and submit the same for confirmation by majority vote of the stockholders in the annual stockholders' meeting. Any renewal or material changes in the terms and conditions of RPTs shall also be approved by the board of directors.

All final decisions of the board on material RPTs, including important facts about the nature, terms, conditions, original and outstanding individual and aggregate balances, justification and other details that would allow stockholders to make informed judgment as to the reasonableness of the transaction, must be clearly disclosed during stockholders meetings and duly reflected in the minutes of board and stockholders' meetings.

- 2.1.3 To delegate to appropriate management committee the approval of RPTs that are below the materiality threshold, subject to confirmation by the board of directors. All decisions under the delegated authority must be properly recorded in the minutes of the committee meetings.

- 2.1.4 To establish an effective system to:

- a. Determine, identify and monitor related parties and RPTs;
- b. Continuously review and evaluate existing relationships between and among businesses and counterparties; and
- c. Identify, measure, monitor and control risks arising from RPTs.

The system shall be able to define related parties' extent of relationship with the CI; assess situations in which a non-related party (with whom a given CI has entered into a transaction) subsequently becomes a related party and vice versa; and

generate information on the type and amount of exposures to a particular related party. The said system will facilitate submission of accurate reports to the regulators/supervisors. The system as well as the overarching policies shall be subject to periodic assessment by the internal audit and compliance functions and shall be updated regularly for their sound implementation. The overarching policy and the system shall be made available to the IC and audit functions for review. Any changes in the policies and procedures shall be approved by the board of directors.

2.1.5 To maintain adequate capital against risks associated with exposures to related parties. In this regard, material risks arising from RPTs shall be considered in the capital planning process. The prescribed scenario/stress tests under the capital planning process shall also capture RPTs in order to determine whether the CI is well-insulated from any going concern issue of related parties.

2.1.6 To oversee the integrity, independence, and effectiveness of the policies and procedures for whistleblowing. The board should ensure that senior management addresses legitimate issues on RPT that are raised. The board should take responsibility for ensuring that staff who raise concerns are protected from detrimental treatment or reprisals.

2.1.7 To constitute an RPT Committee

There shall be constituted an RPT Committee for CIs that are part of an insurance group, financial conglomerates or even mixed conglomerates (group that include non-financial entities) and CIs directed by IC to constitute the said committee.

The RPT Committee shall be composed of at least three (3) members of the board of directors, two (2) of whom shall be independent directors, including the chairperson. The Committee shall at all times be entirely composed of independent directors and non-executive directors, with independent directors comprising majority of the members. In case a member has conflict of interest in a particular RPT, he should refrain from evaluating that particular transaction. The Compliance Officer or Internal Auditor may sit as resource persons in the said Committee.

2.2 Responsibilities of the RPT Committee. The RPT Committee shall:

2.2.1 Evaluate on an ongoing basis existing relations between and among businesses and counterparties to ensure that all related parties are continuously identified, RPTs are monitored, and

subsequent changes in relationships shall be reflected in the relevant reports to the board and regulators/ supervisors.

2.2.2 Evaluate all material RPTs to ensure that these are 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 and that no corporate or business resources of the CI are misappropriated or misapplied, and to determine any potential reputational risk issues that may arise as a result of or in connection with the transactions. In evaluating RPTs, the Committee shall take into account, among others, the following:

- a. The related party's relationship to the CI and interest in the transactions;
- b. The material facts of the proposed RPT, including the proposed aggregate value of such transaction;
- c. The benefits to the CI of the proposed RPT;
- d. The availability of other sources of comparable products or services; and
- e. An assessment of whether the proposed RPT is on terms and conditions that are comparable to the terms generally available to an unrelated party under similar circumstances. The CI shall have in place an effective price discovery system and have exercised due diligence in determining a fair price for RPTs.

All RPTs that are considered material based on CI's internal policies shall be endorsed by the RPT Committee to the board of directors for approval.

2.2.3 Ensure that appropriate disclosure is made, and/or information is provided to regulating and supervising authorities relating to the CI's RPT exposures, and policies on conflicts of interest or potential conflicts of interest. The disclosure shall include information on the approach to managing material conflicts of interest that are inconsistent with such policies; and conflicts that could arise as a result of CI's affiliation or transactions with other related parties.

2.2.4 Report to the board of directors on a regular basis, the status and aggregate exposures to each related party as well as the total amount of exposures to all related parties.

2.2.5 Ensure that transactions with related parties, including write-off of exposures, are subject to periodic independent review or audit process.

2.2.6 Oversee the implementation of the system for identifying, monitoring, measuring, controlling, and reporting RPTs, including the periodic review of RPT policies and procedures.

2.3 Roles of Senior Management and Self-Assessment Functions

2.3.1 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 CI's policy and IC's regulations.

2.3.2. The internal audit function shall conduct a period formal review of the effectiveness of the CI'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.

2.3.3 The compliance function shall ensure that the CI 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 CI'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 CI.

3. Disclosure and Regulatory Reporting

Every CI 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 transactions with subsidiaries and affiliates under existing regulations:

3.1 Insurance/Reinsurance companies, MBAs, Pre-Need and HMOs that are part of a group and conglomerates shall report all entities in the conglomerate structure where it belongs (Annex A). The said structure shall likewise disclose beneficial owners of shareholdings that are in the name of PCD Nominee Corporation. The said report shall be submitted to the IC within 30 calendar days after the end of every calendar year.

3.2 Insurance/Reinsurance companies, MBAs, Pre-Need companies and HMOs shall submit a report on material exposures to related parties, which shall include the material RPTs of their non-financial subsidiaries and affiliates, (Annex B) within 20 calendar days after the end of the

reference quarter. Supervised non-financial subsidiaries and affiliates are therefore expected to report their material RPTs to the parent CI, which in turn shall report the same to IC.

4. Applicability to Branches of Foreign Insurance Companies

The governance principles and requirements embodied in this Circular shall be complied with by branches of foreign insurance companies 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 Circular. Branches of foreign insurance companies are not covered by the reportorial requirement on conglomerate structure.

5. Supervisory Enforcement Actions

The IC reserves the right to deploy its range of supervisory tools to promote adherence to the requirements set forth in these guidelines and bring about timely corrective actions and compliance with IC directives. In this regard, the IC may, among others, issue directives or sanctions on the CI concerned and responsible persons which may include restrictions or prohibitions from certain authorities/activities; and warning, reprimand, suspension, removal and disqualification of concerned CI's directors, officers and employees.

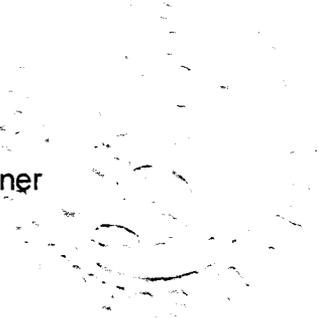
6. Transitory Provision

Every CI, including their financial subsidiaries and affiliates, shall be given six (6) months from effectivity of this Circular to comply with the RPT requirements.

This Circular shall take effect immediately.

For strict compliance.


DENNIS B. FUNA
Insurance Commissioner



Deadline: 30 calendar days after
The end of the calendar
Year

Name of Covered Institutions

Address

Report of Conglomerate Structures

As of _____
(Year-End)

REPUBLIC OF THE PHILIPPINES)
_____) S. S.

I solemnly swear that all matters set forth in this report are true and correct,
to the best of my knowledge and belief.

(Signature of Officer/Alternate)

SUBSCRIBED AND SWORN TO BEFORE ME this _____ day of _____, affiant
exhibiting to me his Community Tax Certificate No. _____ A on _____.

Notary Public
Until December 31, 200 _____
PTR No. _____
Place _____

Doc. No. _____
Page No. _____
Book No. _____
Series of _____

CONGLOMERATE MAP/ORGANIZATIONAL STRUCTURE¹

Name of Covered Institutions

Date

¹ Organizational structure/diagram of the conglomerate.

Deadline: 30 calendar days after
The end of the calendar
Year

Name of Covered Institutions

Address

Report On Material Related Party Transactions

As of _____
(Quarter-End)

REPUBLIC OF THE PHILIPPINES)
_____) S. S.

I solemnly swear that all matters set forth in this report are true and correct,
to the best of my knowledge and belief.

(Signature of Officer/Alternate)

SUBSCRIBED AND SWORN TO BEFORE ME this _____ day of _____, affiant
exhibiting to me his Community Tax Certificate No. _____ A on _____.

Notary Public
Until December 31, 200_____
PTR No. _____
Place _____

Doc. No. _____
Page No. _____
Book No. _____
Series of _____

Material Related Party Transactions

Name of Covered Institutions

Date

Parent/Subsidiary/Affiliate	Related Counterparty	Relationship between the parties	Transaction date	Type of Transaction	Amount	Terms	Rationale for entering into the Transaction
A.Parent							
a. Subsidiaries/Affiliates							
b. DOSRI							
c. Others							
B.Subsidiary 1							
a. Subsidiaries/Affiliates							
b. DOSRI							
c. Others							
C.Subsidiary 2							
a. Subsidiaries/Affiliates							
b. DOSRI							
c. Others							
D.Affiliate 1							
a. Subsidiaries/Affiliates							
b. DOSRI							
c. Others							
E.Affiliate 2							
a. Subsidiaries/Affiliate							
b. DOSRI							
c. Others							

Please indicate in the last column (rationale for entering into the transaction) if the counterparty was a non-related party at the time when the transaction was entered into.