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Anthony McWhirter & Philip Orange

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United States of America **1107**
Kenneth J. Berman, Gregory T. Larkin & Jaime D. Schechter

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Venezuela **1175**
Luisa Acedo de Lepervanche & Manuel Acedo Sucre

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Preface

The genesis of *International Survey of Investment Adviser Regulation* grew out of our day-to-day contact with investment advisers around the world. In 1994, the first edition of this *Survey* covered 18 jurisdictions. We correctly predicted that there would be increased focus on the regulation of investment advisers and, indeed, five years later, the second edition of the *Survey* included 28 countries and the European Union. Since 1999, the explosion in the growth of the world's securities markets, together with the exponential development of international investment management products, such as collective investment vehicles developed to serve individual investors as well as public and private retirement plans, have compelled regulators to respond. This third edition of the *Survey,* which covers investment adviser regulation in 39 countries and the European Union, is evidence of the pace of regulation and the emergence of other relevant laws on the use of electronic media and the Internet, data protection and consumer privacy.

We believe that investment management firms, regulators, legal practitioners and those who study comparative legal systems will find this third edition of the *Survey* to be a valuable resource. Our aim is to foster understanding, development and rationalization of the regulation of investment advisers in a global environment. To that end, the chapters are organized in a manner to facilitate comparisons among and between different legal systems and approaches.

This *Survey* reflects the true dedication of our contributors, to each of whom we express our deepest gratitude for their commitment to this project and their patience with us through the process of publishing this book. The contributing authors are lawyers who are experts in the field of investment management regulation. Each of them has taken the time to share his or her knowledge, practical insights and expertise.

Our assistant editor, Daniel Wiedemann, a senior associate in the firm's Frankfurt office, provided us with invaluable support in organizing the *Survey*

and coordinating with the contributors, as well as in reviewing many of the chapters. Our colleagues in the Investment Management Group of Debevoise & Plimpton, Gregory Larkin and Jaime Doninger Schecter, devoted long hours to the review of many of the chapters in this book. We are truly indebted to each of them for their excellent and important assistance.

Finally, this book could not have been completed without the substantial efforts of the staff in the Frankfurt office of Debevoise & Plimpton LLP. Claudia Naumann supported us throughout the entire process with unfailing professionalism, dedication and good humor, and Anna Gremmers and Abby Carrigan provided important assistance at crucial times.

Marcia L. MacHarg
Kenneth J. Berman

The Philippines

Rafael A. Morales[*]

SyCip Salazar Hernandez & Gatmaitan, Manila

A. OVERVIEW OF THE REGULATORY STRUCTURE

In the Philippines, no single set of laws or regulations governs the activities and operations of investment advisers. Unless specifically subject to Philippine laws and regulations applicable to banks, investment companies or commodity trading advisers, any person or entity (whether Philippine or foreign) may provide investment advice while governed by the rules applicable to business enterprises in general.

1. Applicable Laws and Regulations

1.1. Regulatory Structure

1.1.1. General Banking Law

Subsection 53.4 of Republic Act No. 8791, the General Banking Law of 2000 (the "GBL"), authorizes local banks to act as advisers of investment accounts, with the

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approval of the Monetary Board, the governing body of the *Bangko Sentral ng Pilipinas* (the "Central Bank"). The rules implementing subsection 53.4 of the GBL are set out in Part IV of the Manual of Regulations for Banks (the "Bank Manual").

1.1.2. Investment Houses Law

Investment houses are organized under the Investment Houses Law (the "IHL"), Presidential Decree No. 129 (1973), as amended by Republic Act No. 8366 (1997). The rules implementing the IHL define an investment house as "an enterprise which engages or purports to engage, whether regularly or on an isolated basis, in the underwriting of securities of another person or enterprise, including securities of the Government and its instrumentalities."

An investment house may engage in the business of a dealer or broker under Republic Act No. 8799 (2000) (the "Securities Regulation Code" or "SRC") without obtaining a separate license. An investment house may act as an investment adviser or financial consultant, as well as engage in "such other activities or business ventures as are directly or indirectly related to the dealing in securities and other commercial papers."

1.1.3. Investment Company Act

Section 4(a) of Republic Act No. 2629 (1960), the Investment Company Act (the "ICA"), administered by the Securities and Exchange Commission (the "SEC"), defines an "investment company" as "any issuer which is or holds itself out as being engaged primarily, or proposes to engage primarily, in the business of investing, reinvesting, or trading in securities." Further, the ICA specifically regulates persons or entities that act as advisers of investment companies. Section 3(o) of the ICA defines an investment adviser to an investment company as:

> [A]ny person (other than a bona fide officer, director, trustee, member of an advisory board, or employee of such company as such) who pursuant to contract with such company regularly furnishes advice to such company with respect to the desirability of investing in, purchasing or selling securities or other property, or is empowered to determine what securities or other property shall be purchased or sold by such company.

Any other person that regularly performs substantially all of the duties undertaken by an investment adviser, pursuant to contract with such adviser, will also be deemed an investment adviser to the investment company.

1.2. Role of the Monetary Board

The Monetary Board must license banks and investment houses—which are the Philippine equivalent of investment or merchant banks (see section A.1.1.2)—to engage in investment management activity. The Monetary Board must provide an entity with a favorable recommendation before the entity files with the SEC

articles of incorporation, or amendments thereto, that include the purpose or power to act as managing agent, adviser, consultant or administrator of an investment management, advisory or consultancy account.

2. Registration Requirements

2.1. Activities or Actions Requiring Registration

2.1.1. Investment Management Activity

Section X403.c of the Bank Manual defines ''investment management activity'' as:

> [A]ny activity resulting from a contract or agreement primarily for financial return whereby the bank (the investment manager) binds itself to handle or manage investible funds or any investment portfolio in a representative capacity as financial or managing agent, adviser, consultant or administrator of financial or investment management, advisory, consultancy or any similar arrangement which does not create or result in a trusteeship.

2.1.2. Non-Discretionary Investment Advice

Investment advice, without the discretionary management of investible funds, is excluded from the definition of ''investment management activity.'' Such advice is generally available to any person or entity and not subject to the requirements of the special laws and regulations described herein.

2.2. Definition of Securities

The term ''securities'' is broadly defined in subsection 3.1 of the SRC, as follows:

''Securities'' are shares, participation or interests in a corporation or in a commercial enterprise or profit-making venture and evidenced by a certificate, contract, instrument, whether written or electronic in character. Securities include:

(i) shares of stock, bonds, debentures, notes, evidences of indebtedness, asset-backed securities;
(ii) investment contracts, certificates of interest or participation in a profit-sharing agreement, certificates of deposit for a future subscription;
(iii) fractional undivided interests in oil, gas or other mineral rights;
(iv) derivatives like option and warrants;
(v) certificates of assignments, certificates of participation, trust certificates, voting trust certificates or similar instruments;
(vi) proprietary or non-proprietary membership certificates in corporations; and
(vii) other instruments as may in the future be determined by the SEC.

The above definition would include ''commodity future contracts.'' However, under section 11 of the SRC, the public trading of commodity futures contracts in the Philippines is not allowed, pending the issuance by the SEC of ''rules and regulations involving commodity futures contracts to protect investors to ensure the development of a fair and transparent commodities market.'' To date, the SEC has not issued such rules and regulations.

B. THE AUTHORIZATION PROCESS

1. The Monetary Board

1.1. Banks

Under subsection 53.4 of the GBL, a Philippine bank may be authorized by the Monetary Board to act as ''managing agent, adviser, consultant or administrator of investment management advisory/consultancy accounts.'' For this purpose, the bank normally applies to the Monetary Board for a license to engage in trust and other fiduciary business. Such ''other fiduciary business'' includes investment management activities. Under subsection X404.1 of the Bank Manual, a bank desiring to engage in trust and other fiduciary business must file with the Central Bank an application signed by the bank's president (or officer of equivalent rank) and accompanied by the following documents: (a) a certified true copy of the resolution of applicant's board of directors authorizing the application; and (b) a certification that the applicant has complied with all the conditions prescribed by the Central Bank, including the required capital (which is, for instance, PHP 5.4 billion for a universal bank and PHP 2.8 billion for a commercial bank).

1.2. Investment Houses

In order to engage in investment management activity, an investment house must obtain a license from the Monetary Board to engage in trust and other fiduciary business. An investment house is a locally incorporated company.

If an investment house engages only in investment advising, without the discretionary management of investible funds, the activity does not constitute ''investment management activity.'' Acting purely as an investment adviser, an investment house need not obtain a license from the Monetary Board. Such activity is separately authorized under the IHL (section 7(6)).

Under section 3 of the IHL, an application for registration of the articles of incorporation of an investment house must be accompanied by the following documents:

(i) at least three copies of the proposed articles of incorporation;
(ii) a statement under oath of the educational background and experience of the organizers, directors, and the proposed managerial staff, as well as

information on any position concurrently held by them in other financial or banking institutions, if any;

(iii) a projected statement of assets and liabilities of the proposed Investment House;

(iv) a tentative program of operation for one year, including its investment direction and volume; and

(v) such other information as the SEC may require in support of the application and to enable the SEC to determine the justifiability of establishing the proposed enterprise.

The minimum capital requirement for an investment house is PHP 300 million.

1.3. Other Entities

The Central Bank has unilaterally extended its authority to non-banks by requiring entities other than banks to secure the favorable recommendation of the Monetary Board before filing with the SEC articles of incorporation that include the purpose or power to act as managing agent, adviser, consultant or administrator of investment management, or advisory or consultancy accounts (section 4414Q of the Manual of Regulations for Non-Bank Financial Institutions). The covered purpose or power includes the provision of non-discretionary investment advice as well as the rendering of investment advice to an investment company.

In practice, therefore, and in accordance with law (section 17 of *Batas Pambansa Blg*. 68 (1968), the ''Corporation Code''), the SEC endorses to the Monetary Board the articles of incorporation of any company that wishes to act as an investment adviser. The Monetary Board then conducts a case-by-case review.

As a matter of unwritten policy, the Monetary Board generally provides a favorable recommendation to the SEC so long as the applicant proposes to advise only one entity or perhaps a group of related entities. The Monetary Board will not recommend the articles of an applicant seeking to provide services to more than one entity or group of entities.

The procedure is to obtain first the favorable endorsement of the Monetary Board, prior to filing the articles of incorporation and other incorporation papers with the SEC. Upon receipt of the said endorsement from the Monetary Board, the SEC will officially start the incorporation process.

2. SEC Registration

2.1. How to Register

Any resident corporation designated, or which intends to act, as an investment adviser for an investment company must, before acting as such, file an application with the SEC containing such data and such documents as the SEC will require (see section 2.5 below).

The SEC website (www.sec.gov.ph) contains standard application forms.

2.2. Authorization Process

The SEC will reject an application for registration if the applicant or its principal officer or director:

(i) has willfully made or caused to be made any material false or misleading statement in the application for registration, or willfully omitted any material fact which is required to be stated therein;
(ii) has been convicted of a crime involving moral turpitude and which relates to the purchase or sale of securities, or which arises out of the conduct of the business as a broker, dealer, investment adviser, investment house, bank, trustee or other fiduciary capacity; or
(iii) has willfully violated, or aided, abetted, counseled, commanded, induced or procured the violation by any person of, any provision of the ICA, the SRC or their implementing rules.

2.3. Registration Fees

The initial registration fee is PHP 10,000 plus a legal research fee of PHP 100.

2.4. How Long Does Registration Take?

The registration process can be completed in about one month. However, the SEC may take longer if the application and its supporting documents are not initially in order.

2.5. Information Required

The SEC application solicits disclosure of the following information:

(i) minimum unimpaired net worth of at least PHP 10 million, exclusive of revaluation surplus;
(ii) curriculum vitae of directors; and
(iii) financial statements for at least three years, to the extent applicable.

The SEC may ask the applicant to submit ''such data and such documents'' as it may additionally prescribe.

3. Application of Authorization Requirements to Non-Philippine Advisers

In order to provide investment advice in the Philippines (whether discretionary or not, and whether the advisee is an investment company or not), a non-Philippine

person or entity must establish a business presence in the country. The business vehicle usually chosen is a stock corporation that is either wholly owned by foreigners or a joint venture with Philippine parties. Foreign individuals can be shareholders in that stock corporation. Alternatively, a non-Philippine entity may establish a Philippine branch. In such case, however, the head office will be subject to any liabilities of the branch.

Under the Foreign Investments Act of 1991 (Republic Act No. 7042 (1991), as amended by Republic Act No. 8179 (1996)), the business vehicle chosen to engage in investment advising will be classified as a "domestic market enterprise." The vehicle may be wholly owned by foreigners as long as:

(i) the vehicle does not engage in banking or underwriting activities (which are partly nationalized or reserved to Philippine nationals); and
(ii) the vehicle has paid-in capital of at least USD 200,000.

The minimum capital requirement is reduced to USD 100,000 if the vehicle:

(i) is certified by the Department of Science and Technology as possessing an advanced technology; or
(ii) hires, or issues an undertaking to hire, at least 50 employees.

C. OVERVIEW OF SUBSTANTIVE REGULATION

1. Anti-fraud Provisions and Conflicts of Interest

There are no anti-fraud or conflict-of-interest rules applicable specifically to investment advisers. However, Article 19 of the Philippine Civil Code (Republic Act No. 386 (1950)) generally requires that "every person must, in the exercise of his rights and in the performance of his duties, act with justice, give everyone his due, and observe honesty and good faith." A civil action for damages may be brought for a breach of Article 19.

2. Insider Trading

Insider trading is prohibited by section 27 of the SRC, which makes it unlawful for an insider to sell or buy a security of the issuer if he or she knows a material fact with respect to the issuer or the security that is not generally available to the public. However, no insider trading can be found if:

(i) the insider proves that the information was not gained from his or her being an insider; or
(ii) the other party to the transaction (or his or her agent) is identified, and either: the insider proves that he or she disclosed the information to the other party; or the other party is also in possession of the information.

Insider trading is criminally punishable by a fine ranging from PHP 50,000 to PHP 5 million and/or imprisonment from seven years to 21 years, in the discretion of the court. If the offender is a juridical person, the penalty of imprisonment may be imposed on the officers responsible for the violation. The insider may also be held civilly liable.

3. Disclosures and Other Obligations

Investment managers or advisers authorized by the Monetary Board are subject to reporting and disclosure obligations under the Bank Manual.

Also, in practice, the investment manager or adviser of an investment company performs the reporting functions of such investment company (including, for example, reporting on investments and transactions with its officers, directors or stockholders owning more than 10% of its securities).

Other than as set forth above, there are no rules generally applicable to investment managers or advisers with respect to disclosures and reports to clients and to the public, advertising, recordkeeping, or custody of client assets.

4. Taxation

Investment advisers are not subject to any special taxation or exemption from taxation in the Philippines.

5. Currency for Settlement

Following the repeal of the Uniform Currency Act (1950) by Republic Act No. 8183 (1996), it is now possible for contracting parties to agree to settle obligations or transactions in currencies other than the Philippine Peso.

6. Management of Investment Companies

As noted in section B.2 above, a corporation that proposes to act as an investment adviser to an investment company (either open-end or closed-end) must comply with the requirements under the ICA. Generally, the investment adviser also manages the investment company.

6.1. Corporate Form

The phrase ‘‘any person’’ and the exclusion of certain individuals (e.g., officers, directors and employees) from the definition suggest than an investment adviser can be a natural person. In practice, however, the SEC requires that an investment

adviser to an investment company must be a corporation. For example, such an adviser must have a board of directors.

6.2. Investment Company Service Contract

Pursuant to its service contract, an investment adviser must furnish advice regularly to an investment company with respect to the desirability of investing in securities or other property. This involves a determination of what securities or other property will be purchased or sold by the investment company.

It is unlawful for any person to serve or act as an investment adviser to an investment company, except pursuant to a written contract that:

(i) precisely describes all compensation to be paid thereunder;
(ii) will continue in effect for more than two years from the date of its execution, only as long as such continuance is specifically approved at least annually by the board of directors or by a vote of a majority of the outstanding voting securities of such company;
(iii) may be terminated by any time, without penalty, by the board of directors of the registered company or by the vote of two-thirds of the outstanding voting securities of such company on not more than 60 days' written notice to the investment adviser; and
(iv) provides for its automatic termination in the event of its assignment by the investment adviser.

The contract must not contain any provision that protects or purports to protect the investment adviser against any liability to the investment company or its security holders by reason of willful misfeasance, bad faith or gross negligence in the performance of duties, or by reason of reckless disregard of obligations and duties under such contract.

6.3. Subcontract

If an investment adviser subcontracts substantially all of its duties to another corporation, then such corporation will also be deemed an investment adviser.

6.4. Exclusions

An investment adviser to an investment company, as defined in section 3(o) of the ICA, does not include:

(i) a person whose advice is furnished solely through uniform publications distributed to subscribers thereto;
(ii) a person who furnishes only statistical and other factual information, advice regarding economic factors and trends, or advice as to occasional transactions in specific securities, but without generally furnishing advice or making recommendations regarding the purchase or sale securities;

(iii) a company that furnishes such services at cost to one or more investment companies, insurance companies or other financial institutions;
(iv) any person the character and amount of whose compensation for such services must be approved by a court; or
(v) such other persons as the SEC may determine by rules and regulations or order not to be within the intent of the definition.

7. Commodity Trading Advisers

Commodity trading advisers are subject to a separate set of licensing and operational requirements under the oversight of the SEC. These requirements are to be contained in the rules and regulations of the SEC on the public trading of commodity futures contracts.

D. CONSUMER PRIVACY, ANTI-MONEY LAUNDERING AND DATA PROTECTION

Under the Anti-Money Laundering Act of 2001 (Republic Act No. 9160 (2001) as amended by Republic Act No. 9194 (2003)), banks, investment houses, investment companies, and investment advisers are ''covered institutions'' that are required to submit with the Anti-Money Laundering Council ''covered transaction reports'' and ''suspicious transaction reports.''

A ''covered transaction'' is a transaction in cash or other equivalent monetary instrument involving a total amount in excess of PHP 500,000 within one banking day. There is no threshold amount in a ''suspicious transaction'' but it exists under any of the following circumstances:

(i) there is no underlying legal or trade obligation, purpose or economic justification;
(ii) the client is not properly identified;
(iii) the amount involved is not commensurate with the business or financial capacity of the client;
(iv) taking into account all known circumstances, it may be perceived that the client's transaction is structured in order to avoid being the subject of reporting requirements under the Act;
(v) any circumstance relating to the transaction which is observed to deviate from the profile of the client and/or the client's past transactions with the covered institution;
(vi) the transaction is in a way related to an unlawful activity or offense under the Act that is about to be, is being or has been committed; or
(vii) any transaction that is similar or analogous to any of the foregoing.

The Congress of the Philippines has not yet passed a data protection law. There is, however, a pending bill that seeks to enact the ''Data Privacy Act of 2011.'' This is

to protect "individual personal information in information and communications systems in the government and the private sector."

E. ENFORCEMENT

The Central Bank is responsible for administrative supervision over those engaged in investment management activities and may enforce the provisions of the GBL and the Bank Manual either administratively or through judicial proceedings. The Central Bank may initiate proceedings against an investment manager or its principal officers or majority stockholders. Violations of the provisions of the GBL or its implementing rules (including the Bank Manual) are punishable by a fine not more than PHP 200,000, imprisonment for not more than ten years, or both.

At the same time, the SEC enforces the provisions of the ICA and the SRC and the rules adopted under such laws. The SEC may proceed either administratively or through judicial proceedings.

Violations of the ICA or its implementing rules are punishable by a fine of not more than PHP 50,000 or imprisonment for not more than five years, or both. Violations of the SRC or its implementing rules (including the provision on insider training) are subject to a fine of not less than PHP 50,000 nor more than PHP 5 million, imprisonment of not less than 7 years nor more than 21 years, or both. If the offender is a corporation or other legal entity, the penalty will be imposed upon the officer responsible for the violation. Moreover, if such officer is not a Philippine citizen, he or she will, in addition to the penalties prescribed, be deported without further proceedings after serving his or her sentence.

F. EXTRATERRITORIAL APPLICATION

The foregoing laws and regulations have no extraterritorial application.