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### **CIRCULAR LETTER**

**TO : (1) PRE-NEED COMPANIES**  
**(2) ENTITIES AUTHORIZED TO ENGAGE IN TRUST**  
**OPERATIONS AND ACT AS TRUSTEE FOR PRE-NEED**  
**CORPORATIONS**

**SUBJECT : ALLOWABLE INVESTMENTS FOR PRE-NEED TRUST**  
**FUNDS**

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#### **Section I. Mandate and Objectives**

Pursuant to Sections 6 and 34 of Republic Act No. 9829, otherwise known as the Pre-Need Code of the Philippines, the Insurance Commission issues these guidelines to Pre-need Corporations and entities authorized to sell pre-need plans:

To provide an updated and more flexible choice of investments for the trust fund subject to rules and regulations that would ensure prudent investment management and protection of the interest of the planholders.

#### **Section II. Scope**

These Guidelines shall cover other allowable investments for pre-need plans.

### **Section III. Definitions**

For purposes of this Circular, the term:

- A. "Trust Fund" shall mean a fund set up from the planholder's payments to pay for the cost of benefits and services, termination values payable to planholders and other costs necessary to ensure the delivery of benefits or services to planholders as provided for in the contracts.
- B. "TOAP" refers to the Trust Officers Association of the Philippines.
- C. "Trustees" is defined as any bank, investment house, or a stock corporation, duly authorized by the monetary board to engage in trust, investment management, and fiduciary businesses which has an existing trust agreement with a pre-need company.
- D. "Commission" refers to the Insurance Commission.
- E. "Other Investments" shall mean investments not expressly defined in Section 34 of the Pre-Need Code.
- F. "BSP" refers to the Bangko Sentral ng Pilipinas.
- G. CAMELS Rating of the BSP shall mean the soundness of a bank measured on a scale of 5 (strongest) to 1 (weakest). The rating is based on the adequacy and quality of a bank's Capital, Assets, Management, Earnings, Liquidity, and Sensitivity. These ratings are disclosed only to the bank's management and not to the general public.
- H. "SEC" refers to the Securities and Exchange Commission.
- I. "Interest Rate" shall mean the average yield of the trust fund over the last 10 years.
- J. "Equities" shall mean the buying and holding of shares of stock on a stock market by individual and firms in anticipation of income from dividends and capital gains, as the value of the stock rises.
- K. "Real Estate Investment Trust" or "REIT" is a stock corporation established in accordance with the Corporation Code of the Philippines and the rules and regulations promulgated by SEC principally for the purpose of owning income-generating real estate assets.

L. "Service Assets" are investments by a pre-need company directly or through a service provider in resources or capabilities that may be used to offset or manage future liabilities. These are assets or shares that are not intended primarily for Resale or Investment but to offset future liabilities.

M. "Corporation Code" refers to Batas Pambansa Bilang 68, otherwise known as the Corporation Code of the Philippines.

Whereas Section 4 of the Pre-Need Code provides, the terms not otherwise defined under this Code shall be construed in their usual and commonly understood trade, business, commercial or investment meaning.

#### **Section IV. Other Investments**

In addition to the provisions of Section 34 of the Pre-Need Code, Investment of the Trust Fund, the following additional investment outlets shall be allowed as Other Investments with corresponding maximum limits and subject to prior approval of the Commission. The amount allocated for this purpose shall not exceed twenty percent (20%) of the total trust fund while the investment in any particular item below shall not exceed fifteen percent (15%) of the trust fund. Provided, further, that no investment in any single entity shall exceed ten percent (10%) of the total value of the trust fund.

- a) **Preferred Shares.** Preferred stock, also called **preferred shares, preference shares**, or simply **preferreds**, is a special equity security that has properties of both an equity and a debt instrument and is generally considered a hybrid instrument. Preferreds are senior (i.e., higher ranking) to a common stock but are subordinate to bonds. Preferred stock usually carries no voting rights, but may carry a dividend and may have priority over common stock in the payment of dividends and upon liquidation.
- b) **Real Estate Investment Trust (REIT).** "Real Estate Investment Trust" or REIT as defined under Republic Act 9856 is a stock corporation established in accordance with the Corporation Code of the Philippines and the rules and regulations promulgated by the Commission principally for the purpose of owning income-generating real estate assets. For purposes of clarity, a REIT, although, designated as a "trust" does not have the same technical meaning as "trust" under existing laws and regulations but is used herein for the sole purpose of adopting the internationally accepted description of the company in accordance with global best practices.
- c) **Tier 2 Notes.** Tier 2 notes that generally constitute direct, unconditional, unsecured and subordinated obligations of a bank. More commonly, claims of all Noteholders will enjoy priority over the rights and claims of holders of all classes of equity securities of a bank, including holders of preference shares, if any. The issuer bank should have a credit rating of no less than "A" from Philrating.

- d) **Service Assets.** Under Republic Act 9829 Section 35. Responsibilities of the Trustee of the Pre-Need Code under (c.) "Not use the trust fund to invest in or extend any loan or credit accommodation to the pre-need company, its directors, officers, stockholders and related interests as well as to persons or enterprises controlling, owned or controlled by, or under common control with said company, its directors, officers, stockholders and related interests except for entities which are direct providers of pre-need companies.

Service Assets are investments by a Pre-need Company directly or through a Service Provider in Resources or Capabilities that may be used to offset a future liability. These are assets or shares which are not intended for Resale or Investment but to offset future liabilities.

- i. Pre-need Companies differ from Insurance Companies because their obligations are not necessarily financial in nature. Some of their liabilities may be in the form of Assets or Services. Hence there are Arbitrage opportunities where the Pre-need Company is able to provided the Service or Asset at a cost below the amount originally projected in the financial model.
- ii. Mortuaries – Historically investments by Pre-need Companies in Mortuaries have allowed some Pre-need Companies to answer their Life Plan obligation. Investments take the form of buying or investing in Mortuaries, purchasing assets required to provide Memorial Services, such as Hearses, Cremation Machines or loaning funds to independent Mortuaries where conditions of the loan include providing discounted Memorial Services.
- iii. Memorial Lots and/or Columbaries—Some Life Plan liabilities are in the form of Memorial Lots or Columbaries, where the commitment of the Life Plan company is to provide a complete Funeral Service including a Memorial Lot.

Memorial lots or columbaries that are not part of the package of a funeral service shall be considered as inventories held for sale. In which case, the asset shall be considered as real estate.

- iv. Schools – Investments by Pre-need Companies in Educational Institutions would reduce the cost of servicing Education Plans, because the cost of educating additional students is only marginal. The Pre-need Company would only have to spend on the marginal cost of educating additional students.

- v. Retirement Homes – Some Pension Plans may include the provision of Adult Oriented Housing for Retirees as a benefit of the Pension Plan. Consequently, the ownership of such Service Assets will inoculate or control the liability of the Pre-need Company.

TOAP may recommend other assets not defined above from time to time subject to approval of the Commission.

It is clear that based on the commercial definitions of “Preferred Shares”, “REIT”, “Tier 2 Notes”, “Service Assets or shares in Service Providers”, they are not “Fixed Income Instruments” as defined under Section 34(a) or “Equities” as defined under Section 34(b) nor “Real Estate” as defined under Section 34(c) of the Pre-Need Code.

#### **Section V. Clarification on Bonds and Bangko Sentral ng Pilipinas – Special Deposit Account (BSP-SDA)**

##### **a. Peso Denominated Bonds and other evidence of indebtedness issued by:**

- d.1) Supranationals (or international organizations whose membership transcends national boundaries or interests, e.g. International Bank of Reconstruction and Development, Asian Development Bank).
- d.2) Corporate bonds of privately-owned domestic corporations duly registered with the Securities and Exchange Commission (SEC) with a credit rating of at least “A” by an accredited Philippine rating agency.

The maximum exposure to corporate bonds shall not exceed fifteen percent (15%) of the total trust fund amount while the exposure to each issuance shall not exceed ten percent (10%) of the allocated amount.

##### **b.) Bangko Sentral ng Pilipinas – Special Deposit Account (BSP-SDA)**

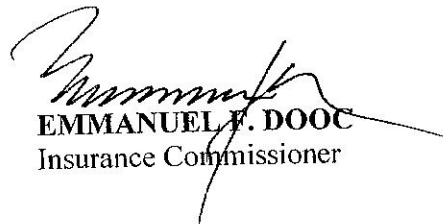
BSP-SDA facility consists of fixed-term deposits by banks and by trust entities of banks and non-bank financial institutions with the BSP. It is not guaranteed by the Republic of the Philippines but a stand alone credit of the BSP. This shall be allowed as short-term investment.

This shall not be considered as an alternative investment in government securities as prescribed in Section 34 (a) (1) of the Pre-Need Code.

## **Section VI. Method of Disclosure of Required Information**

Under the present provisions of Chapter X of the Pre-Need Code, all pre-need companies must strictly comply with the following disclosures:

- A. Annual Pre-Need Reserve Valuation Report as stated in Section 41 of the Pre-Need Code.
- B. Annual Audited Financial Statements Fund as stated in Section 42 of the Pre-Need Code.
- C. Annual Statement of Trust Fund as stated in Section 43 of the Pre-Need Code.
- D. Publication of Annual Statement Fund as stated in Section 44 of the Pre-Need Code.

  
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Insurance Commissioner