

# TRANSLATION

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## Republic of Panama Superintendency of Banks

**RULE N° 11-2017**  
(dated 26 December 2017)

**“Whereby the guidelines for Derivatives Operations are established”**

**THE BOARD OF DIRECTORS**  
in use of its legal powers and,

### **WHEREAS:**

Due to the issuance of Decree Law 2 dated 22 February 2008, the Executive Branch re-edited Decree Law 9 dated 26 February 1998 and all its amendments as a consolidated text, and this text was approved by means of Executive Decree 52 dated 30 April 2008, hereinafter referred to as the Banking Law;

Pursuant to the provisions of paragraphs 1 and 2 of Article 5 of the Banking Law, safeguarding the soundness and efficiency of the banking system and strengthening and fostering favorable conditions for the development of the Republic of Panama as an international financial center are objectives of the Superintendency of Banks;

Pursuant to paragraph 5 of Article 11 of the Banking Law, establishing the administrative interpretation and scope of the legal provisions and regulations on banking matters is a technical duty of the Board of Directors of the Superintendency of Banks;

Trading with derivatives has increased exponentially, both in the volume of trading of common derivatives such as forwards, options and interest rate swaps, credit derivatives and currency options, as well as in the volume of trading of complex derivatives such as structured notes and structured credit products;

The increasing complexity of these instruments and operations is a critical risk factor, since it affects relevant aspects of the banks' financial risk management;

During its working sessions, the Board of Directors determined it necessary and advisable to establish regulatory prudential standards for promoting and fostering bank best practices in managing derivatives.

### **RESOLVES:**

#### **CHAPTER I**

#### **SCOPE AND DEFINITIONS**

**ARTICLE 1. SCOPE.** This Rule is applicable to:

1. State-owned banks;
2. General license banks;
3. International license banks.

**ARTICLE 2. DEFINITIONS.** For the purposes of this Rule, the following terms will be understood as follows:

# TRANSLATION

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1. **Derivative:** A financial instrument whose market value is dependent upon one or more underlying assets. Its settlement is made at a future date, i.e. other than the date in which the agreement was entered into. This settlement can be made in cash, financial instruments or in tradable products or assets, as agreed upon in the contract or the relevant regulations for the securities trading system, trading operations records or the asset compensation and settlement system.

A derivative permits administering or taking one or more risks related to the underlying assets and meets one of the two (2) options below:

- a. It does not require an initial net investment;
  - b. It requires an initial net investment below that is needed to purchase instruments providing the same expected payment as a response to changes in market factors.
2. **Forward:** An over-the-counter (OTC) contract where two counterparties agree on the exchange, at a future date, of a certain amount of a specific product (stocks, bonds, currencies, commodities) for a price originally determined in the contract;
  3. **Forward rate agreement (FRA):** An OTC contract settled in cash at a future date, based on a notional value, a market interest rate, a reference deadline and a fiscal year interest rate agreed to on the date the contract was negotiated. The settlement is determined on the difference of interests calculated on the notional value, with the market interest rate and the agreed interest rate and with regard to the reference deadline. The contract also describes how the market interest rate is determined;
  4. **Financial futures:** A financial contract in which both counterparties agree on the exchange, at a future date, of a given amount of a specific product for a determined price. Futures are forwards traded on the stock exchange by means of standardized contracts regarding quantity and deadline. Future contracts are settled on a daily basis through the stock exchange with income and losses for the contract counterparties. The most common underlying assets are commodities, fuel, currencies, interest rates, stocks and stock ratios. There are various potential deadlines to trade contracts but each traded contract has a single deadline. Stock exchange regulations determine the nature and amount of the surety the parties must provide and the rules for balancing the surety with the risk factor;
  5. **Interest swaps:** Contracts traded in OTC markets where both parties agree on an exchange of cash at certain agreed dates, on a generally equal, notional value defined in the contract, related to the interest calculated at a fixed interest rate agreed to in the contract against interest calculated with a market interest rate determined throughout the swap life. The interest amount is determined by the notional value, by the applied interest rate and the corresponding deadline for each interest settlement period;
  6. **Currency swaps:** Currency swap contracts traded in OTC markets where the parties agree on the exchange of a certain amount of cash in different currencies on the dates established in the contract until the deadline. The amounts of cash usually correspond to interest, calculated with the types of interest of each currency and according to what is established in the contract. The notional values employed for the calculation of interest are originally determined by the type of exchange counted from the transaction date. The notional value is usually exchanged when the contract is concluded;
  7. **Options:** Contracts in which rights but not obligations are purchased on cash flows at future dates or its equivalent. The rights seller does have the obligation if the buyer executes the right. The rights refer to receiving an amount of cash at one or various future dates or the power to purchase or to sell certain financial instruments with a price established in the contract, at one or various future dates. The price of rights is called a premium or option premium. Options are traded both

# TRANSLATION

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in stock exchanges as well as in OTC markets. There is a great variety of options and the most traded are defined below:

- 7.1. **Standard European option (vanilla):** There are two modalities, the call option and the put option. In the standard European call option, the purchaser buys the option to purchase a quantity of a determined product with a price (exercise price) established in the contract, on the expiration date. In the standard European put option, the buyer buys the right to sell a quantity of a certain product with an exercise price established in the contract, on the expiration date.
- 7.2. **Standard American option:** This option differs from the European option in that the option exercise it is not limited to the option expiration date, but can be exercised on any business date from the option trading date until the expiration date.
- 7.3. **Standard Bermudan option:** The right is the same as in the standard European option, except that the settlement can be demanded on a number of intermediate dates between the dates permitted in the American and European options.
- 7.4. **Exotic option:** Any option that differs from those mentioned above is called an exotic option. The most important are listed below:
  - a. **Digital option:** Settled by a fixed amount, determined on the trading date. The digital options may be call or put, according to the right executed when the underlying variable has a value greater than the exercise value or when the underlying variable has a value below the exercise value, both on the contract expiration date.
  - b. **Range option:** Settled by a fixed amount, determined on the trading date. The option is executed if the underlying variable on the contract expiration date is within a range of values determined on the option trading date.
  - c. **Asian price average option:** Settled according to the underlying instrument price average. The average is defined either as an arithmetic average or a geometric average. The frequency (daily, weekly, monthly, among others) for the average calculation is defined in the contract.
  - d. **Asian exercise price average option:** The exercise price is defined on the expiration date by means of the arithmetic or geometric price average. The frequency (daily, weekly, monthly, among others) for the average calculation is defined in the contract.
  - e. **Lookback option:** Settled on the expiration of the maximum (or minimum) reached by the underlying asset in a given period of time.
  - f. **Barrier option:** The settlement of the option is the same as in the standard European option, but is subject to an additional condition, called a barrier, which is a specific level of the underlying variable determined in the contract. There are many different modalities of barrier options. The key aspect is in the fact that the right of exercise is conditioned on the underlying variable behavior, on whether or not it reaches a barrier.
  - g. **Basket option:** The settlement is based on the weighted average of different underlying assets.
  - h. **Exchange option:** An asset is exchanged for another during the settlement.

# TRANSLATION

- i. **Quanto option:** An option settled in a currency other than the one in which the underlying financial instrument is nominated at an exchange rate determined on the original contract date.
8. **Credit derivatives:** Credit derivatives are contracts that allow the protection buyer to transfer the credit risk of a given underlying instrument or of an underlying instrument portfolio to the protection seller without selling the underlying instrument. Usually, but not necessarily, the buyer is the owner of the underlying instrument.

The most traded credit derivative is the credit default swap that has one single underlying instrument. The protection buyer periodically pays the protection seller an amount called the contract premium, which is the result of multiplying the contract nominal value by a determined percentage, until the expiration date of the contract, or until the credit event happens in the terms defined in the contract. In the latter case, the contract is settled either by the seller paying the nominal price in cash to the buyer and the buyer's delivery of the underlying instruments to the seller at the same notional value, or it is settled by the protection seller paying the protection buyer the difference between the notional contract value and the market price of the underlying instruments in cash.
9. **Structured financial instruments:** Structured financial instruments are contracts whose cash flows can be reproduced by a portfolio formed by traditional financial instruments and derivative instruments, called implicit derivatives. Traditional financial instruments generally are debt instruments with fixed or variable coupons or without coupons (zero coupon instruments), while derivatives tend to be options, generally exotic options. Structured instruments sometimes are traded under the name of exotic options that are implicit in the instrument's financial structure. Structured financial instruments are also called hybrid products.
10. **OTC markets:** Over-the-counter (OTC) markets are markets in which financial instruments are traded outside the stock exchange environment. Usually there are market creators establishing supply and demand prices. The most important OTC markets are interbank markets and currency markets. OTC contracts are bilateral contracts between the parties, although there are master contracts (e.g. the International Swaps and Derivatives Association, ISDA) to benefit the legal security of transactions.
11. **Market value of the financial instrument:** The amount for which a financial asset can be delivered or a financial liability can be settled between independent parties acting for their own benefit (IFRS 39, IFRS 9). The best evidence of market value will be the market price of this instrument traded in an active market. For financial instruments with an inactive market, valuation techniques will be used. To establish the price would have been active market-like conditions.
12. **Active market:** A financial instrument is considered listed in an active market if the listing prices are easily and regularly available through a stock exchange, financial intermediaries, financial institutions, price services or regulatory bodies, and these prices show real market transactions made regularly between the parties acting in conditions of reciprocal independence.
13. **Derivatives risk:** A position in a derivative instrument exposes the entity to specific risks, whose nature and force depends on the use (hedging, trading, intermediation) the entity assigns to the derivative. The most important risks are:
  - 13.1. **Counterparty risk:** The risk of losses due to the counterparty not complying with its contractual obligations, both on the derivative contract itself as well as on the contribution and replacement of guarantees.
  - 13.2. **Market risk:** The risk of losses due to negative changes in the contract valuation, both throughout the contract as well as on liquidation.

# TRANSLATION

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- 13.3. **Liquidity risk:** The risk of losses due to the inability to close a position due to the absence of counterparties, or due to negative changes in the market prices when trying to open or close a contract.
- 13.4. **Operating risk:** The risk of losses due to operating events, such as mistakes in the registration, accounting, valuation of contracts, calculation of guarantees, and mistakes in risk measurement. The legal risk is very important for derivatives, especially in the contracts marketed to customers.
- 13.5. **Reputational risk:** The risk of losses due to reputational deterioration that could originate from bad management of the derivative or claims from customers that have suffered losses with derivatives or structured products marketed by the entity.

The definitions included herein are examples of the most common derivatives and are not an exhaustive and exclusive list.

## CHAPTER II

### RESPONSIBILITIES AND RISK MANAGEMENT

**ARTICLE 3. CORPORATE GOVERNANCE.** The Board of Directors of the Bank conducting operations with derivatives and structured products must assume, at a minimum, the following responsibilities:

1. Approve the precise objectives the entity seeks in trading derivatives, as well as establishing the role derivatives play in the overall strategy of the bank's business, distinguishing between:
  - a. Its own positions for the purpose of obtaining benefits in the short term;
  - b. Derivatives positions for the purpose of obtaining coverage for a determined risk;
  - c. Derivatives positions as counterparty to client positions, where the entity takes the contrary position, taking some type of risk;
  - d. Investment positions in structured products which include implicit or explicit derivatives;
2. Approve the bank's policies and manuals on managing derivatives and structured products, including a risk profile consistent with the bank's strategy. The job position manual must establish the specifics of the various duties and the relevant coordination tasks among those duties;
3. Ensure that the internal regulations on derivatives and structured products and the policies on limits are effectively incorporated into daily practices at the bank and that there is an independent internal control permitting this incorporation;
4. Authorize the use or investment in new derivatives and structured products and establish prudential limits, ensuring that the systems essential to supporting the new operations and sufficient technical capacity within the different functional areas are in place before implementation;
5. Approve the organizational structure for managing derivatives and structured products, including an effective and independent internal control system with enough [top management] support to perform its duties and the necessary independence from the business areas;
6. Know and understand the bank's risk exposure in trading with derivatives and structured products.

# TRANSLATION

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The top management of banks trading with derivatives must assume, as a minimum, the following responsibilities:

1. Develop and propose policies for managing derivatives and structured products;
2. Implement strategies and policies approved by the Board of Directors on derivative instruments and structured products;
3. Understand the risk levels taken by the bank in trading with derivatives and structured products;
4. Maintain an organizational structure for managing derivatives and structured products clearly assigning responsibilities, authority and hierarchy;
5. Establish procedures ensuring the appropriate and timely flow of information on exposures to derivatives and structured products among the different departments involved;
6. Ensure objectives, procedures and controls are functioning, effective and complied with in managing derivatives and structured products;
7. Guarantee the establishment of training and updating programs for the staff involved in managing derivatives and structured products;
8. At market closing each day, the information on the position in the different contracts, on income and losses, both in valuations and in traded positions, and on the estimated risk taken according to the different types of risks and their compliance with defined tolerance levels, must be made available to top management.

The auditing or internal control department of each bank is responsible for checking and monitoring compliance with all of the requirements established herein.

**ARTICLE 4. COMPREHENSIVE RISK MANAGEMENT.** Within its comprehensive risk management, the bank must include all the risks related to trading derivatives, paying special attention to the following issues:

1. The valuation of the derivatives as the starting point for most of the risks related to trading derivatives that the bank must manage; therefore, the weaknesses on the valuation side should be considered in risk identification, measurement, management and control;
2. When measuring market risk, the liquidity factor must be considered to prevent risk undervaluation;
3. Counterparty risk management requires its appropriate identification and measurement and the implementation of the guarantees and collateral policies appropriate to the exposure to the risk taken. Furthermore, [it also requires] following up on the guarantee valuation and the procedures for adjusting the guarantee valuation for changes in the value of both in the derivative and the collateral itself;
4. Banks must identify operating risks and design appropriate policies to neutralize their effects. Particularly, they must pay special attention to legal risks related to the interpretation and compliance with contracts, registration risks, operations accounting and model risks, both in risk valuation and measurement, to name the most important;
5. It is necessary to strengthen the risk and internal control unit to identify, with the greatest accuracy, the type of use the bank gives derivatives and the bank's level of exposure to the different risks.

# TRANSLATION

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**ARTICLE 5. POLICIES AND PROCEDURES FOR MANAGING RISKS WITH DERIVATIVES.** The policies and procedures for managing risks with derivatives must be in writing, and the documents must be sufficiently precise and disclosed in those areas of responsibility considered appropriate. The directors must ensure that the policies accurately define the responsibilities and also establish the different duties and interrelationships among the different areas or departments related to the development and operation of derivatives.

## CHAPTER III

### REQUIREMENTS AND VALUATION OF DERIVATIVES

**ARTICLE 6. MINIMUM COMPLIANCE REQUIREMENTS FOR THE INCORPORATION OF THE DERIVATIVES AND/OR STRUCTURED PRODUCTS IN THE BALANCE SHEET.** Banks including derivatives and/or structured products in their balance sheets must have the capability to evaluate the relevant contract and measure the risks. Furthermore, depending on the business model, the banks must strictly comply with the following:

1. Establish procedures to ensure, in a timely manner, that all of the financial derivatives and structured products used are authorized both by the applicable legal framework and the internal policies, and that they are also established in written contracts (contracts in the case of derivative financial instruments in the OTC market) and are duly documented, confirmed and registered;
2. Have the technical capacity and technology instruments to assess and manage derivatives risks within the entity's portfolio;
3. Data processing, risk management and assessment systems must be appropriately supported and controlled, along with a contingency plan for the recovery of the information, particularly in unexpected situations;
4. To have and to put in practice a Board of Directors-approved manual containing the policies and procedures for all business models of the entity, and specific [policies and procedures] for the various derivatives and structured products used by the entity. This manual must be updated periodically and must include all of the mandatory points herein and must have, as a minimum:
  - a. General policies for contracting derivatives and structured products;
  - b. Valuation methodologies and procedures used by the bank, including sources of information on the different required parameters, as well as the relevant technical remarks for these methodologies and procedures;
  - c. Methodologies for the identification and measurement of each of the risks found in each type of contract;
  - d. Registration, accounting and management information systems for each contract, describing the necessary specifications;
  - e. Risk concentration limits for the derivatives portfolio;
  - f. Risk control or mitigation tools and techniques to be used;
  - g. Methodologies for the calculation of potential losses under different scenarios, including stress testing;
  - h. Rules and procedures for the management of guarantees when using derivatives;
  - i. Any other relevant aspect that, in the bank's judgment, is required to use these instruments.

# TRANSLATION

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5. For derivatives traded in OTC markets, banks must necessarily enter into a master agreement with the parties clearly establishing the duties and/or obligations of both parties;
6. They must put in place a regular training and updating program for traders, support staff, risk follow-up areas and, in general, for all staff involved in managing and controlling derivatives and/or structured products;
7. The policy on limits must include the risk related to changes in market value, as well as counterparty, liquidity and concentration risks for derivatives. Limits must be included in the policies before taking any position and there must be support documentation thereof.

**ARTICLE 7. ADDITIONAL REQUIREMENTS THAT BANKS USING DERIVATIVES FOR TRADING MUST COMPLY WITH.** The banks trading derivatives aimed at obtaining short-term benefits must have clearly defined policies and procedures to conduct these operations. These policies and procedures must include, as a minimum:

1. A documented, differentiated trading strategy for each type of instrument and differentiated portfolio, approved by the board of directors, including the expected maintenance horizon for portfolio positions;
2. Defined policies and procedures for actively managing the portfolio, described in the manuals designed for that purpose. The manuals will be made available to the Superintendency of Banks at all times and will include the following features:
  - a. The management must be made by a specialized area;
  - b. Position limits must be set consistent with the level of risk taken. Furthermore, they must be continually reviewed to ensure their suitability and a strict control system must be established in order to ensure compliance with the limits;
  - c. Positions will be revalued at their market value on a daily basis;
  - d. Estimation and calibration of parameters used for valuation and risk management techniques must be frequently evaluated;
  - e. The board of directors of the bank must be frequently informed on the positions of the different instruments by means of a standardized information system;
  - f. Conduct an active follow-up on the positions including the evaluation of market liquidity and the hedging capacity of positions. The follow-up will include, among others, the evaluation of the quality and availability of data obtained from the market to assess the market trading volume and the profits on traded positions.
3. Control policies and procedures on the positions maintained relative to the entity's trading strategy.

**ARTICLE 8. DERIVATIVES ACCOUNTING.** All derivatives will be registered at the market value. Furthermore, trading derivatives must be differentiated in the accounting books from the hedging derivatives used by the entity to manage risks.

**ARTICLE 9. MARKET VALUE ESTIMATION IN MARKETS WITH LESS LIQUIDITY OR NO LIQUIDITY.** The valuation of derivatives and structured products must be governed by the following criteria where there is no price market:

1. The cash flow of the structured financial instrument must be segregated in such a way that it is possible to identify individual financial instruments that can be used to replicate those cash flows;

# TRANSLATION

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2. Each discreet financial instrument identified in the structured instrument must be assessed using a generally accepted specific model that includes all of the risk factors that determine the market value;
3. Obtain an interest payment structure for the types of risk-free zero coupon instruments, in order to obtain the prices of zero coupon instruments that will permit updating the cash flow for each instrument;
4. The estimated market value for each individual component of the structured instrument must include all of the necessary adjustments to show the different risks in the instrument's cash flow, particularly the adjustments related to estimating counterparty risk.
5. The valuation methodology must be properly documented in such a way that supervisors can reproduce the results obtained.

**ARTICLE 10. REQUIREMENTS RELATED TO THE VALUATION PROCESS.** Banks must establish and maintain appropriate systems and controls that ensure prudent and reliable valuation estimates. These systems and controls will include the following elements, as a minimum:

1. Documented policies and procedures on the valuation process containing a clear description of the responsibilities of the different departments participating in this process and the sources of market information used to conduct the valuation, as well as an analysis of the adequacy of each of them, the frequency of independent valuations, the temporary sequence of closing prices, the procedures for adjusting the valuations, the procedures for verification at the end of the month and the procedures for verification to be established for specific purposes;
2. The department responsible for the valuation process must be independent of the trading units. Additionally, the submittal of required information for the derivatives valuation, as well as the valuation results, must be submitted through direct channels, independent of the trading areas. This information channel must include the Assets and Liabilities Committee and the Risk Committee;
3. Banks must apply the estimate method chosen to all cases. To the extent possible, it is important to check whether the results obtained by a certain method are significantly different from those obtained by other traders, because international accounting standards give preference to generally-used methods;
4. The models used, both for valuation and risk measurement, must be subject to regular examination in order to determine the reliability of the results;
5. The models developed by the banks themselves must be designed by a unit independent of the trading tables and must be approved by the entity indicated by the board of directors. Banks must implement formal procedures to review and control future model modifications. There must be a registration and a file of the models used, and of the reviews conducted. The file must include, as a minimum, the following: mathematical specification of the model, the assumptions used, the sources of information used to estimate model parameters and examples clearly showing how model results are obtained.

**ARTICLE 11. VALUATION FREQUENCY.** Positions will be valued at market prices at least daily. There should be a centralized valuation system established, independent of the trading tables.

**ARTICLE 12. AUTHORIZATION FOR THE USE OF NEW TYPES OF DERIVATIVES.** Banks must include the process for authorizing trading with new derivatives in the derivatives risk management policies.

Within the trading authorization process for new derivatives, the body responsible for authorizing the new products and the processes to be followed before the new product can be used by the bank must be perfectly defined. In addition, the approval of new products must

# TRANSLATION

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include the opinions and preparation of the bank's risk control, operations, accounting, legal advisory, internal auditing and business (front office) areas.

The authorization to trade new products requires an in-depth review of systems, including technology systems, to analyze the degree of adjustment needed for the new requirements. The most important factors to be considered are:

1. Whether the new product requires a new valuation methodology;
2. Capital requirements demanded by present or future regulations;
3. Legal and regulatory restrictions that can affect the operation of the new instrument;
4. The characteristics of the market in which the product will be negotiated;
5. Counterparty risk and an estimate of other risks;
6. Price formulation and whether broad market information exists on cost and prices;
7. Required technology development;
8. Preparation of the registration, administration and control systems to monitor the new instrument.

**ARTICLE 13. SYSTEM OF LIMITS.** The activity with derivatives must be subject to limits not dependent on the nature of the derivative. These limits must be consistent with the bank's measurement of risk, the entity's risk strategy and the risk tolerance defined by the board of directors. Limits should be determined for market, liquidity, counterparty and concentration risk. These limits must be approved by the board of directors and consistently applied.

The main limits to be considered are:

1. Those determined by the maximum intraday exposure and the next-day exposure for each business unit;
2. The limits for the set of derivatives activities;
3. The limits for valuation losses;
4. The limits for aggregate losses in a determined period of time for each business unit and for all units together;
5. The limits for counterparty risk;
6. The limits for concentration risks differentiated by instruments, markets and counterparty.

**ARTICLE 14. SIGNIFICANT LOSSES.** Significant losses in the bank relative to the risk profile, equity and utilities immediately requires:

1. A review of trading strategies;
2. An evaluation of trader skills;
3. A review of limit determination systems;
4. A review of risk models;
5. A review of control systems;
6. A review of authorization systems for taking derivatives positions.

# TRANSLATION

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Once the above actions have been conducted, the bank must make sure it takes the necessary corrective actions to mitigate risks and additional future losses.

**ARTICLE 15. APPROVAL FOR EXCEEDING ESTABLISHED LIMITS.** The approval for exceeding limits must be an exceptional option that must be based on a previously approved procedure. Furthermore, there must be a new limit imposed above the limit being exceeded. The continued approval for exceeding limits is a bad practice that must be rejected.

**ARTICLE 16. TRADING REGISTRATION AND ADMINISTRATION SYSTEMS.** Internal procedures must appropriately establish the distribution of duties for all areas in such a way that they fully cover the process for registration, valuation and accounting of trading operations.

Registration systems must include all relevant variables that feed the systems for the valuation, accounting, risk calculation, monitoring and settlement of contracts.

**ARTICLE 17. INTERNAL CONTROL FOR MONITORING DERIVATIVES TRADING.** The banks must have an independent internal control unit, in this case the risk management unit that is directly connected to top management and is appropriate for the sophistication and complexity of the derivatives positions the bank maintains regularly. In particular, the education and experience of the internal control staff must be in keeping with the duties performed. The internal control area must have the necessary technology resources to perform its duties.

The main objectives of the internal control unit within the scope of derivatives instruments are:

1. Verify that all positions opened with explicit or implicit derivatives correspond to the modalities authorized by the internal regulations of the entity;
2. Check that operations are properly registered in the information systems established for that purpose and accurately valued and registered.
3. Ensure that all risks of the derivatives activity are disclosed, identified, equipped with the metric that corresponds to their level of complexity, are efficiently managed according to the standards and procedures established and have an information system that matches the needs of the different operational levels of authorized users;
4. Ensure that the entity meets the required capital requirements and that it meets the information requirements established by the Superintendency of Banks.

Lastly, Internal Auditing is responsible for checking all processes and other controls herein.

## CHAPTER IV

### INFORMATION REQUIREMENTS

**ARTICLE 18. DISCLOSURE OF INFORMATION ON DERIVATIVES TO THE MARKET.** In the financial statements notes, the banks will disclose the information on derivatives they deem relevant to the market, including, as a minimum:

1. The notional volume and market value of derivatives differentiated according to the nature of the instrument, the currency, the term, the purpose for which the financial entity contracted it and the type of information used to estimate the market value, distinguishing it on three levels:
  - a. Prices listed in active markets;
  - b. Direct or indirect observable inputs;
  - c. Non-observable inputs.

# TRANSLATION

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2. If the entity has used valuation models and techniques to obtain the market value, it should disclose the following information:
  - a. If there is a choice of valuation techniques and how the choice is made;
  - b. The risks or deficiencies (if any) in the valuation technique chosen;
  - c. If there were changes in the valuation technique since the last date of submittal of financial statements, the grounds for making the changes;
  - d. The description of the use of market listings or price-setting services;
  - e. When prices of similar instruments are used to measure the reasonable market value, how this prices are adjusted to reflect the characteristics of the instruments being measured should be explained;
  - f. When there are adjustments to model values due to factors the model does not evaluate, what those factors are and how the adjustments are made;
  - g. A description of the facts and circumstances that led to the determination that the market is active or inactive.

**ARTICLE 19. SUBMITTAL OF INFORMATION.** Banks must submit the information referred to herein to the Superintendency of Banks in the form and frequency it may determine.

## CHAPTER V

### PENALTIES

**ARTICLE 20. PENALTIES.** Failing to comply with the provisions herein will be penalized according to the provisions of Title IV of the Banking Law.

## CHAPTER VI

### FINAL PROVISIONS

**ARTICLE 21. ENACTMENT.** This Rule will enter into effect on the second (2<sup>nd</sup>) day of January, two thousand nineteen (2019).

Given in the city of Panama on the twenty-sixth (26<sup>th</sup>) day of December, two thousand seventeen (2017).

**FOR COMMUNICATION, PUBLICATION AND ENFORCEMENT.**

**THE CHAIRMAN,**

**THE SECRETARY,**

L.J. Montague Belanger

Nicolas Ardito Barletta