Republic of the Philippines
Department of Finance
Securities and Exchange Commission
SEC Building, EDSA, Greenhills, Mandaluyong City

In the matter of:
Petition for Declaration of a State of Suspension of Payments; For the Approval of a Rehabilitation Plan; and the Appointment of A Management Rehabilitation Committee

VICTORIAS MILLING CO., INC.
Petitioner-Appellant,

\- **Versus -** **SEC En Banc Case No. 04-15-368**
(SEC Case No. 07-97-5693)

EAST WEST BANKING CORP.,
Movant-Appellee.

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DECISION

Before the Commission *En Banc* is an *Appeal*[1] filed on 06 April 2015 by VICTORIAS MILLING COMPANY, INC. (**Appellant VMC**) seeking to reverse and set aside the SPECIAL HEARING PANEL I (**SHP1**) *Order* dated 19 March 2015 (**Assailed Order**) resolving in favor of EAST WEST BANKING CORP. (**Appellee EWBC**) the latter's *Motion to Compel Victorias Milling Corporation (sic) to Allow EWBC to Exercise its Option for the Conversion of the Uncontroverted Convertible Note (CN)*[2] (**Motion to Compel**).

Appellant VMC is a domestic corporation registered with the Commission on 07 May 1919 with SEC Registration No. PW-364. It is engaged in raw and refined sugar manufacturing[3].

Appellee EWBC is a domestic corporation registered with the Commission on 22 March 1994 with SEC Registration No. AS094-002733. It is engaged in universal/commercial banking[4].

Facts of the Case

On 04 July 1997, Appellant VMC filed before the Commission, through the Securities Investigation and Clearing Department (SICD) a *Petition for Declaration of*

[1] Notice of Appeal and Memorandum of Appeal dated 06 April 2015.
[2] Dated 05 November 2015.
[3] VMC's 2015 General Information Sheet (GIS).
[4] EWBC 2014 GIS.

Suspension of Payments; for the Approval of a Rehabilitation Plan; and the Appointment of a Management Committee (SEC Case No. 07-97-5693). The SICD gave due course to the said petition. Thereafter, the SICD issued an *Order* dated 08 July 1997 that suspend all actions or claims against Appellant VMC pending before any court, tribunal, office, board and/or the Commission.

A Rehabilitation Plan proposed by the Management Committee of Appellant VMC was approved in an *Order* dated 02 June 1999 by the SICD, later amended on 17 August 1999, and further modified on 19 August 1999. In an *Order* dated 29 November 2000, the Alternative Rehabilitation Plan (**ARP**), as proposed by the VMC Management Committee, was approved by the SICD[5].

Thereafter, Appellant VMC and its creditors, including Appellee EWBC, executed a *Debt Restructuring Agreement* (**DRA**)[6] dated 29 April 2002. It was agreed that as a debt restructuring measure, Appellant VMC will issue long-term commercial papers or debt securities in the form of *Convertible Notes* (**CN**) in favor of its bank creditors.

As a result, Appellant VMC issued on 01 September 2003 a CN with PN No. 898303000211 in favor of Appellee EWBC, whereby the former promises to pay the latter the amount of Php 200,396,734.00 at the rate of Eight Percent (8%) per annum on 01 September 2018, subject to some terms and conditions set forth therein[7].

On 31 May 2013, Appellant VMC was able to settle all its "Restructured Loans". As a result, it had to pay/redeem the CNs it issued pursuant to the ARP and DRA to the extent of its Cash Flow in excess of Capital Expenditure[8].

On 24 February 2014, Appellant VMC notified Appellee EWBC, through a letter[9], that its Board of Directors on 20 February 2014 has approved the partial payment/redemption in the amount of Php 187,299,930.26[10] for the CN it issued[11] pursuant to Section 13.2[12] of the DRA (Mandatory Pre-payment). Such action is aligned with Appellant VMC's efforts to further strengthen its financial viability and to ensure its ability to comply with the terms of the DRA. However, on 28 February

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[5] SEC Case No 07-97-5693, *Order* dated 29 November 2000 – WHEREFORE, the proposed Alternative Rehabilitation Plan of the MANCOM is hereby APPROVED as presented. Its implementation is likewise ordered in accordance with the Order of this Commission dated June 2, 1999, August 17, 1999 and August 19, 1999, insofar as they are consistent with the herein approved ARP. SO ORDERED.

[6] Annex "W" of the Motion to Compel.

[7] Annex "D" of the Memorandum of Appeal.

[8] Paragraph 2.15. of the Rejoinder.

[9] Dated 24 February 2014.

[10] Php 101,823,763.10 [Amount of CN to be paid/redeemed] + Php 85,476,167.16 [Interest computed as of February 28, 2014 (gross of tax)].

[11] Annex "A" of the Answer.

[12] Section 13.2 of the DRA - In the event that the Restructured Loans are fully settled before the 15 year repayment period, VMC Cash Flow in excess of Capital Expenditure requirements shall be used to pay/redeem the Convertible Note (principal plus accumulated interest).

2014, Appellee EWBC informed Appellant VMC that the former decided not to accept the offer of partial payment/redemption[13].

Thereafter, Appellant VMC and Appellee EWBC exchanged correspondences invoking and enforcing their respective rights under the DRA and CN. Appellee EWBC communicated to Appellant VMC that it has a right to convert the CN into equity as provided therein. While, Appellant asserts its right to redeem the CN and is prepared to pay the stated amount with interest.

On 27 March 2014, Apellee EWBC's Board of Directors approved the sale of the CN. In a letter dated 31 March 2014[14], Appellee EWBC informed Appellant VMC of the said approval and in fact it commenced the required publication as required by Section 16(k) of the DRA[15].

In a letter dated 31 March 2014[16], Appellant VMC informed Appellee EWBC that on 28 March 2014, it disclosed to the Philippine Stock Exchange (PSE) that Appellant VMC Board of Directors approved the payment/redemption of the CN up to 600 million Pesos pursuant to the ARP and DRA.

On 02 April 2014, Appellant VMC informed Appellee EWBC, in a letter dated 26 March 2014[17], that a two percent (2%) creditable withholding tax shall be deducted on the interest payment of the CN. Appellant VMC also presented the partial redemption checks dated 28 February 2014 in the amount of Php 170,258,258,92 and Php 15,397,761.55 or a total of Php 185,656,020.47. Appellant VMC threatened Appellee EWBC that should it refuse the delivery payment, it shall file the necessary action in court, including the consignment of the redemption amount.

In a letter dated 02 April 2014[18], Appellee EWBC reiterated its position that it will not accept Appellant VMC's partial offer of redemption and returned the two Metrobank checks which the latter presented.

On 03 April 2014, Appellee EWBC reiterated again to Appellant VMC that the former's Board of Directors has approved the sale of its Appellant VMC CN and

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13 Paragraph 2, of the Answer.

14 Annex "E" of the Answer to the Memorandum of Appeal dated 23 April 2014.

15 Section 16 (k) of the DRA – Right of First Refusal of Noteholders and Stockholders: In the event that a noteholder decides to sell its Convertible Notes, said selling noteholder shall first offer its Convertible Notes to the other stockholders and existing stockholders. **The offer to sell shall be by publication in a newspaper of nation-wide circulation for at least seven (7) calendar days at the expense of the selling noteholder.** If no other noteholder or existing stockholder decides to buy the Convertible Note subject of the sale within three (3) working days after the seventh (7th) day of publication, the selling noteholder may then offer the Convertible Note to a third party. The buyer of the Convertible Note shall then convert the Convertible Notes into common shares of VMC, subject to the conversion schedule provided for in the Convertibility Feature discussed above.

16 Annex "G" of the Answer to the Memorandum of Appeal dated 23 April 2014.

17 Annex "H", id.

18 Annex "I", id.

published on March 30-31, 2014 and April 1-5, 2014[19], the required notice to all noteholders and existing stockholders of Appellant VMC.

In a letter dated 03 April 2014, Appellant VMC transmitted the final payment/redemption of the VMC NC (principal plus interest) in the amount of Php 180,469,879.70[20].

In summary, Appellant VMC made the the following offer of payment/redemption[21]:

Date Received & Returned by EWBC	Date of Letter of VMC	Attached Check	Date of Check	Amount of Check
April 2, 2014	March 26, 2014	Metrobank check no. 370038109 Metrobank check no. 370038	February 28, 2014 February 28, 2014	P170,258,258.92 P15,397,761.55
April 2, 2014	April 1, 2014	PNB check no. 001645504	April 4, 2014	P89,982,086.08
April 4, 2014	April 3, 2014	Metrobank check no. 3700383152	April 4, 2014	P180,469,879.70

However, Appellee EWBC refused to accept the Appellant VMC's offer of redemption and returned the payments for the same.

In a letter dated 25 September 2014, Appellant VMC consigned to Atty. Luis Ma. G. Uranza, *Rehabilitation Receiver of VMC*, the following amounts as payment/redemption the CN, to wit[22]:

Check No.	Date	Amount
3700383154	August 26, 2014	Php 185,656,020.47
3700383155	September 23, 2014	Php 180,469,879.70
	Total	Php 366,125,900.17

On 15 October 2014, Appellee EWBC notified Appellant VMC, through a letter[23], that it is exercising its option to convert thirteen percent (13%) of the latter's

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19 Affidavit of Publication dated April 2014 by Evelyn S. Arevalo, The Manila Times,, Annex "G" of the Motion to Compel.
20 May 31, 2014.
21 Paragraph 3.11 of the Memorandum of Appeal, Paragraph 13 of the Answer.
22 Letter dated 25 September 2014 to Rehabilitation Receiver, Annex "E" of the Memorandum of Appeal.
23 Dated 14 October 2014.

Outstanding Unconverted CN in accordance with Section 16(h)[24] of the DRA and paragraph 5[25] of the CN.[26]

On the same day, Appellant VMC informed Appellee EWBC, through a letter[27], that there is no outstanding CN issued to the latter and that the CN issued has already been paid/redeemed. The checks issued by Appellant VMC for the payment/redemption have been consigned with the Rehabilitation Receiver for custody since Appellee EWBC refused to accept the same[28].

On 11 November 2014, Appellee EWBC filed a *Motion to Compel* with the SHP1 seeking to compel Appellant VMC to convert the CN to the latter's common shares up to the extent thirteen percent (13%) of Appellee VMC's outstanding CN.

SHP1 gave due course to Appellee EWBC's motion and on 19 March 2015, it issued the *Assailed Order* to wit:

> "We agree with the contention that it is mandatory for VMC to pay/redeem the Convertible Notes as enunciated in Section 13.2 of the DRA and paragraph 5 of the ARP. However, we disagree with VMC's contention that it is equally mandatory for EWBC to receive and accept the same.
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> As explicitly provided in the ARP, as well as in Section 13.2 of the DRA the mandatory tenor of the provisions pertains only to VMC. As worded, it is VMC which is mandated to pay/redeem the CNs. There is nothing in the provisions relied upon, either express or implied, that mandate or obligate the CN holders, like herein EWBC, to accept the payment/redemption offer of VMC.
>
> To this effect, the Hearing Panel rules that contrary to the allegation of VMC, the mandatory provisions of the ARP and Section 13.2 of the DRA apply only to VMC's payment/redemption of the CN and not to EWBC's acceptance of the same.
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[24] Section 16(h) of the DRA - The Convertible Notes shall be converted at the option of the holders thereof into common shares of VMC at a ratio of one (1) Convertible Note to One (1) common share of VMC xxx. (vi) After the Fifth Conversion Period, a maximum of thirteen percent (13%) of the Outstanding Unconverted Convertible Notes may be converted per year from the eighth (8th) year to the fourteenth (14th) year. The Convertible Notes may be converted within a period beginning on the thirty-first (31st) day after the end of each succeeding year from the Fifth Conversion Period and shall expire sixty (60) days thereafter. The term "Outstanding Unconverted Convertible Notes" is defined as the principal amount of the Convertible Notes outstanding as of the ninety-second (92nd) day after the end of the seventh (7th) year."

[25] Paragraph 5 of the CN "The Holder has the right and option to convert this Note into common shares of the Issuer during the designated periods xxx.

[26] Annex "F" of the Memorandum of Appeal; Annex "M" of the Answer.

[27] Dated 15 October 2014.

[28] Annex "G" of the Memorandum of Appeal, Annex "N" of the Answer.

To give emphasis to the provision of paragraph 8 of the CN, the conversion of the CN into common shares of the Issuer at the option of the Holder during the conversion period shall prevail over the exercise by the Issuer of its option to redeem this Note. This contractual provision of the CN is the main basis of EWBC's assertion of its superior right to convert. Thus, on the issue of whether or not EWBC can rightfully demand for the conversion of the CN to VMC shares, the answer is in the affirmative.

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This Hearing Panel agrees with EWBC. If we look further at the provision of Section 16(h)(vii) of the DRA, which both VMC and EWBC have not given much attention to, 'Any or all Convertible Notes which were not converted during the previous conversion period may be converted within a period beginning on the sixtieth (60^{th}) day before the end of the fifteenth (15^{th}) year from the Issue Date and shall expire thirty (30) days thereafter (the "Final Conversion Period")'. In this case, EWBC's exercise of option to convert the CN was made on 14 October 2014, which is well within the 5^{th} conversion period.

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Considering all the foregoing, EWBC's Motion is hereby GRANTED subject to the following condition:

1. Adoption of a Board Resolution authorizing/confirming the refusal to accept the payment/redemption of the Convertible Note by VMC and the exercise of its right to convert the CN into VMC common shares;

Further, VMC is hereby directed to convert 13% of the outstanding unconverted convertible note held by EWBC into VMC common shares within fifteen (15) days from presentation to it of the Board Resolution.

SO ORDERED."

Hence, this *Appeal*.

On 06 April 2015, Appellant VMC filed the instant *Appeal*[29] with the Commission *En Banc*, asserting the following errors:

1. SPH1 committed a grave and patent error when it ruled that the Mandatory Provisions of the ARP and Section 13.2 of the DRA apply only to VMC's payment/redemption of the EWBC convertible note and not to EWBC's acceptance to the same;

[29] Dated 06 April 2015.

2. SPH1 committed a grave and patent error when it ruled that EWBC could demand the conversion of the EWBC convertible note to VMC common shares despite the fact that VMC, in accordance with the provisions of the ARP, DRA, and EWBC convertible note had already paid/redeemed the EWBC convertible note way before the applicable conversion period which was from October to November 2014;
3. SPH1 committed a grave and patent error when it disregarded the fact that the payment/redemption period by VMC of the EWBC convertible note pursuant to the ARP and/or under Section 13.2 of the DRA is consistent with the objectives of a corporate rehabilitation;
4. SPH1 committed a grave and patent error when it failed and/or refused to deny the motion to compel despite its ruling that a Board Resolution indicating the authority of EWBC to refuse payment/redemption of the EWBC convertible note and to exercise its right to convert the EWBC convertible note into common shares of VMC is necessary.

In an *Order* dated 07 April 2015, the Commission *En Banc* ordered Appellee EWBC to file its *Reply Memorandum* to the Appellant VMC's appeal. On 24 April 2015, Appellee EWBC filed an *Answer to the Memorandum of Appeal (Re: Order dated March 19, 2015 issued by the Special Hearing Panel 1 of the Securities and Exchange Commission)*[30]. This is treated as Appellee EWBC's *Reply Memorandum*.

Appellee EWBC, in its *Answer*, argues that:

1. The ARP, DRA and EWBC's CN do not contain any provision to the effect that it is mandatory for EWBC to accept the redemption offered by VMC;
2. VMC's tender of payment to the Rehabilitation Receiver representing the redemption payment is ineffective;
3. EWBC's exercise of its right to convert is not inconsistent with the objective of the VMC's corporate rehabilitation;
4. Non-submission of Board Resolution cannot be used as a basis for denying EWBC's exercise of its right to convert the CN;
5. The instant appeal is procedurally flawed since it violated Section 12-1 of the 2006 SEC Rules of Procedure (2006 Rules).

On 11 May 2015, Appellant VMC filed a *Rejoinder*[31] refuting all the allegations and arguments of Appellant EWBC, to wit:

1. The Mandatory Provisions of the ARP and Section 13.2 of the DRA apply to VMC's payment/redemption of the EWBC Convertible Note and to EWBC's acceptance of the same;

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[30] Dated 23 April 2015.
[31] Dated 11 May 2015.

2. VMC, in accordance with the provisions of the ARP, DRA and EWBC Convertible Note, had already fully paid/redeemed the EWBC Convertible Note way before the applicable conversion period, which was from October 1 to November 29, 2014;
3. Payment/Redemption by VMC of the EWBC Convertible Note pursuant to the ARP and/or under Section 13.2 of the DRA is consistent with the objectives of a corporate rehabilitation;
4. The issuance of secretary's certificate did not cure the acts of EWBC in refusing payment/redemption of VMC;
5. The instant appeal is procedurally proper under all circumstances.

On 12 May 2015, Appellee EWBC filed a *Supplemental Answer to the Memorandum of Appeal*[32] arguing the following:

1. The right to convert is a property right purchased by holders of the Convertible Notes through substantial and valuable consideration, while the option to redeem was granted without any consideration. Hence, the former right is superior to the latter option;
2. VMC's exercise of its right to redeem is only "final and irrevocable" insofar as it is concerned but does not bind the holder of the CN should it choose to exercise its right to convert during the conversion period. The right to convert must be considered as superior at all times to the option of redemption, otherwise the right to convert becomes illusory;
3. The Conversion of EWBC's CN is in furtherance of the objectives of the rehabilitation plan. It is even beneficial to VMC's financial condition;
4. The absence of a Board Resolution specifically authorizing EWBC to refuse payment for and to convert its CN into shares was not necessary. Even assuming without admitting that it was, the execution of Board Resolution thereafter authorizing such an act legally ratifies the same.

Thereafter, on 28 May 2015, it filed a *Sur-rejoinder*[33] to Appellant VMC's *Rejoinder* rebutting the allegations and arguments of Appellant EWBC, to wit:

1. The option of VMC to redeem the CN in this case is governed by Section 16(i) not Section 13.2 of the DRA. Hence, VMC was required to use externally raised equity funds to redeem the CN, which was not what happened in this case;
2. Mutuality of Contracts was not violated by the ruling of the Special Hearing Panel. What is applicable to the case and what was upheld is the principle of autonomy of contracts;
3. Superiority of the Right to Convert is a crucial provision in the CN and the DRA. It cannot simply be rendered inapplicable by VMC at

[32] Dated 11 May 2015.
[33] Dated 28 May 2015.

its discretion. Hence, the exercise of EWBC's option during the conversion period was valid and enforceable.

On 26 June 2015, Appellant VMC filed an *Ex-Parte Motion to Resolve*[34] praying for the early resolution of its appeal with the Commission *En Banc* because any delay would constrain Appellant VMC to pay unwarranted interest under the CN.

Issue/s

The issues raised can be summarized into one which is: Whether or not Appellant VMC's exercise of its right to redeem/pay the EWBC Convertible Note proper based on the terms and conditions of the Approved Rehabilitation Plan, Debt Restructuring Agreement and EWBC Convertible Note.

Ruling

Before we resolve the case on the merits, we first resolve a procedural issue raised by Appellee EWBC on the mode of review availed by Appellant VMC.

Appellee EWBC argues that the *Assailed Order* emanated from the SPH1. Thus, Appellant VMC should have filed a *Petition for Review on Certiorari*[35] (Certiorari) as a mode of review and not an ordinary *Appeal*[36] as provided under the 2006 SEC Rules of Procedure (2006 Rules).

On the other hand, Appellant VMC argues that it is stated in Section 6.2[37] of the 2006 Rules that decision of Special Hearing Panels are appealable to the Commission *En Banc* and that a *Certiorari* is only available if there is no appeal, nor any plain, speedy and adequate remedy in the ordinary course of law. Appellant VMC also argues that there is no violation of the 2006 Rules because the *Appeal* it filed is still compliant with the requirements for a *Certiorari*.

Appellee EWBC's contention on this procedural matter is without merit. An *Order* from SPH1 is appealable to the Commission En Banc either through a *Petition for Review on Certiorari* or an *Ordinary Appeal*. The Commission *En Banc* on

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[34] Dated 24 June 2015.

[35] Sec. 12-1. Petition for Review on Certiorari. When any Hearing Officer/Panel of the Commission, has acted without or in excess of its jurisdiction, or with grave abuse of discretion <u>and there is no appeal, nor any plain, speedy and adequate remedy in the ordinary course of law</u>, a person aggrieved thereby may file a verified petition with the Commission En Banc alleging the facts with certainty and praying that judgment be rendered annulling or modifying the proceedings of such Hearing Officer or Panel and granting such relief as the applicable laws may require.

[36] Section 11-1. Ordinary Appeal. An appeal to the Commission En Banc may be taken from a decision, order, or resolution issued by an Operating Department if there are questions of fact, of law, or mixed questions of fact and law.

[37] Section 6.2 of the 2006 Rules - Finality of Decision. The Decision of the Hearing Panel or Officer, in the absence of a timely appeal, shall become final and executory upon entry in the Book of Entry of Judgment.

several occasions have previously ruled that orders or resolutions by Special Hearing Panels can be appealed using the two above-stated modes.

Moreover, the 2006 Rules should be liberally construed in order to promote public interest and assist the parties in obtaining a just, prompt, expeditious and inexpensive resolution, settlement, and/or disposition of all actions brought before the Commission and to carry out the objectives of the laws it is mandated to implement[38].

The foregoing considered, we now resolve the case on the merits based on the allegations and arguments contained in the *Appeal* and supported by substantial evidence.

The instant *Appeal* has merit.

Article 1306 of the New Civil Code provides that "**the contracting parties may establish such stipulations, clauses, terms and conditions as they may deem convenient**, provided they are not contrary to law, morals, good customs, public order, or public policy".

In the case of *Bricktown Development Corp. vs. Amor Tierra Development Corp.*[39], the Supreme Court ruled that:

> "**A contract, once perfected, <u>has the force of law between the parties</u>** with which they are bound to comply in good faith and from which neither one may renege without the consent of the other. **The autonomy of contracts allows the parties to establish such stipulations, clauses, terms and conditions as they may deem appropriate** provided only that they are **not contrary to law, morals, good customs, public order or public policy**. The standard norm in the performance of their respective covenants in the contract, as well as in the exercise of their rights thereunder, is expressed in the cardinal principle that the parties in that juridical relation must act with justice, honesty and good faith."

In interpreting contracts, the Supreme Court has ruled in the case of *Benguet Corporation, et al. v. Cesar Cabildo*[40] that:

> "The cardinal rule in the interpretation of contracts is embodied in the first paragraph of Article 1370 of the Civil Code: "[i]f the terms of a contract are clear and leave no doubt upon the intention of the contracting parties, the **literal meaning of its stipulations shall control**." This provision is akin to the "**<u>plain meaning rule</u>**" applied by Pennsylvania courts, which assumes that the intent of the parties to an instrument is "**embodied in the writing itself, and when the words are**

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[38] Section 1-3., 2006 Rules.
[39] G.R. No. 112182, December 12, 1994.
[40] G.R. No. 151402, August 22, 2008, citing Abad v. Goldloop Properties, Inc., 521 SCRA 131, 143-145 (2007).

clear and unambiguous the intent is to be discovered only from the express language of the agreement." It also resembles the **"four corners" rule, a principle which allows courts in some cases to search beneath the semantic surface for clues to meaning.** A court's purpose in examining a contract is to interpret the intent of the contracting parties, as objectively manifested by them. The process of interpreting a contract requires the court to make a preliminary inquiry as to whether the contract before it is ambiguous. A contract provision is ambiguous if it is susceptible of two reasonable alternative interpretations. **Where the written terms of the contract are not ambiguous and can only be read one way, the court will interpret the contract as a matter of law. If the contract is determined to be ambiguous, then the interpretation of the contract is left to the court, to resolve the ambiguity in the light of the intrinsic evidence.**

Thus, to determine as to who has a better right between Appellant VMC's right to redeem the CN and Appellee EWBC's right to convert the CN, we need to carefully examine and interpret the stipulations in the agreements (ARP, DRA and CN) as agreed by the parties in its entirety.

Part (IV) of the ARP provides that the approved quasi-reorganization of Appellant VMC will reduce the par value of its stocks from P10/Share to P1.0/Share and it will increase its Authorized Capital Stock (ACS) to 4,605,086,296 shares. From the new ACS, 1.1 billion (1,100,000,000) shares shall be issued in favor of its clean creditors who will convert their respective unpaid interest plus part of the principal into common shares. The remaining unissued shares of 3,009,128,626 shall be reserved for the P2,400,000,000 convertibles notes. [41] Further, pargraph 5(b) part (IV) of the ARP provides "should the P3.055 Billion restructured debt be fully settled before the 15-year repayment period, VMC cash flow shall in excess of Capital Expenditure requirements shall be used to pay/redeem the convertible notes (principal plus accumulated interest)".

Further, Section 1.2 of the DRA states that from a total of 7.9 Billion Pesos Outstanding Loan Obligation of Appellant VMC, it shall be divided as follows;

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[41] ARP, (IV), paragraph 1 - Proposed Amendment to the Original Rehabilitation Plan (in case of bidding failure)
1. Capital Structure/Debt Conversion
The approved quasi reorganization of VMC where the par value will be reduced from P10/Share to P1.0/Share will remain. The Authorized Capital Stock will be increased to 4,605,086,296 shares instead if the original approval of 2,563,035,708 share (inclusive of the P1.5 Billion Convertible Notes). From the new authorized capital stock, 495,957,670 will be issued to existing VMC share-holders "or at the rate of 2.91 shares for every one (1) existing share held". The balance of 1,100,000,000 shares shall be issued in favor of the clean creditors who will convert their respective unpaid interest plus part of the principal into common shares. Said unpaid interest is estimated to be P957,919,187 by April 30, 2000 the balance of P142,080,813 will come from the outstanding principal due to the non-MTI creditors.
The remaining unissued shares of 3,009,128,626 shall be reserved for the P2,400,000,000 convertible notes and the proportionate share of the RSDO claims in the case the SEC recognizes them as clean credits equivalent to VMC's clean loans. The proportionate shares are estimated to be 405,310,466 out of the P630 Million principal claim and P203,818,160 unpaid interest as of April 30, 2000.

1. 1.1 Billion of the Outstanding Loan Obligation shall be converted into equity for clean creditors;
2. **2.4 Billion will be converted into Convertible Notes in favor of creditors;**
3. The remaining balance will be restructured over a Fifteen (15) year period from effectivity of the DRA. [42]

The aforesaid P2.4 billion CNs shall be subject to terms and conditions provided under the subsequent provisions of the DRA, to wit:

> "***Section 13 – Mandatory Pre-payment***
>
> 13.1 In the event VMC's Net Cash Flow at the end of a crop year exceeds the Projected Net Cash Flow for that particular crop year as provided for in its Approved Rehabilitation Plan, VMC shall pre-pay in inverse order (last maturities first) the Restructured Loans without penalty equal to Seventy Five Percent (75%) of the incremental Net Cash Flow. The term Net Cash Flow is defined as Net Income After Tax plus Depreciation Charges plus Other Non-Cash Charges.
>
> 13.2 **In the event that the Restructured Loans are fully settled before the 15 year repayment period, VMC Cash Flow in excess of Capital Expenditure requirements shall be used to pay/redeem the Convertible Note (principal plus accumulated interest)**.
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> ***Section 16 – Conversion of P2.4 Billion worth of Outstanding Loan Obligation into Convertible Notes***
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> 16. As a debt reduction measure and as part of capital infusion feature of the Approved Rehabilitation Plan, **VMC shall issue at least Two Billion Four Hundred Million Pesos (P2.4 Billion) worth of long-term commercial papers or debt securities in the form of Convertible Notes**, under the following terms:
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> x x x x x x x x x
>
> **(h) Convertibility Feature:**
> **The Convertible Notes shall be converted at the option of the holders thereof into common shares of VMC at a ratio of one (1)**

[42] "Out of the total Outstanding Loan Obligations, a total of P1.1 billion shall be converted into equity, **P2.4 billion into convertible notes in accordance with the Terms of Issuance of Convertible Notes** provided under Sections 16 and 17 hereof and the remaining balance in the amount of x x x (PhP 4,417,292,827.45), shall be restructured over a Fifteen (15) year period from the effectivity of this Restructuring Agreement as specified in Section 36 hereof (the "Restructured Loan"). x x x"

Convertible Note to One (1) common share of VMC, <u>subject to the following schedule</u>:

(i) Maximum of Twenty Percent (20%) of the original Issue Amount of the Convertibility Notes may be converted within a period beginning on the thirty first (31st) day after the end of the third (3rd) year from Issue Date and shall expire sixty (60) days thereafter (the "***First Conversion Period***");
(ii) Maximum of Twenty Percent (20%) of the original Issue Amount of the Convertibility Notes may be converted within a period beginning on the thirty first (31st) day after the end of the fourth (4th) year from Issue Date and shall expire sixty (60) days thereafter (the "***Second Conversion Period***");
(iii) Maximum of Twenty Percent (20%) of the original Issue Amount of the Convertibility Notes may be converted within a period beginning on the thirty first (31st) day after the end of the fifth (5th) year from Issue Date and shall expire sixty (60) days thereafter (the "***Third Conversion Period***");
(iv) Maximum of Twenty Percent (20%) of the original Issue Amount of the Convertibility Notes may be converted within a period beginning on the thirty first (31st) day after the end of the sixth (6th) year from Issue Date and shall expire sixty (60) days thereafter (the "***Fourth Conversion Period***");
(v) Any or all outstanding converted Convertible Note which were not covered during the First, Second, Third, and Fourth Conversion Periods may be converted within a period beginning on the thirty first (31st) day after the end of the seventh (7th) year from Issue Date and shall expire sixty (60) days thereafter (the "***Fifth Conversion Period***");
(vi) <u>After the Fifth Conversion Period, a maximum of Thirteen Percent (13%) of the Outstanding Unconverted Convertible Note may be converted per year from the eighth (8th) year to the fourteenth (14th) year. The Convertible Notes may be **converted within a period beginning** on the thirty first (31st) day after the end of each succeeding year from the Fifth Conversion Period and **shall expire sixty (60) days thereafter.**</u> The term "Outstanding Unconverted Convertible Notes" is defined as the principal amount of the Convertible Notes outstanding as of the ninety-second (92nd) day after the end of the seventh (7th) year, and
(vii) Any or all Convertible Note which were not converted during the previous conversion periods may be converted within a period beginning on the sixtieth (60th) day before the end of the fifteenth (15th) year from Issue Date and shall expire thirty (30) days thereafter (the "***Final Conversion Period***").

The aggregate amount of Convertible Notes that may be converted into common shares of VMC shall not exceed Twenty Percent (20%) of the original Issue Amount of the Convertible Notes for each year covering the conversion period beginning the third (3rd) year to the sixth (6th) year.

For the period beginning the eighth year to the fourteenth (14th) year, the annual aggregate amount of Convertible Notes that may be converted into common shares of VMC shall not exceed Thirteen Percent (13%) of the Outstanding Unconverted Notes.

(i) Redemption at the Option of VMC (Call Option):
VMC may redeem the Convertible Notes at any time at Issue Price plus accrued interest beginning at the end of the third (3rd) year from the Issue Date and ending on Redemption Date which is at the end of the fifteen (15) years from Issue Date; Provided that, VMC shall use externally raised equity funds such as from rights offering. The application of the raised equity funds shall be as follows:
(i) Seventy Percent (70%) for the redemption of the Convertible Notes, pro-rata among holders; and
(ii) Thirty Percent (30%) for the pre-payment of the Restructured Loans of the SECURED CREDITORS (first mortgage-creditors) covered by the existing Mortgage Trust Indenture, pro-rata among lenders.

From the foregoing, Appellant VMC issued CNs in favor of its bank creditors as provided by the DRA. These CNs shall be redeemed by Appellant VMC in two ways: 1.) Mandatory Pre-payment[43]; and 2.) Call Option[44]. On the other hand, it is clear from Section 16(h) of the DRA that the CNs issued can be converted by the bank creditors into common shares of VMC at a ratio of one (1) CN to one (1) common share of VMC[45] only during designated conversion periods[46].

Pursuant to the DRA, Appellant VMC issued on 01 September 2003 a CN in favor of Appellee EWBC which the latter accepted[47]. The issued CN provides that Appellant VMC promises to pay Appellee EWBC on 01 September 2018, the principal amount of Php 200,396,734.00 at the rate of Eight Percent (8%) per annum[48] subject to the following terms and conditions, among others:

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43 Section 13.2 of the DRA – Mandatory Pre-payment.
44 Section 16(i) of the DRA – Redemption at the Option of VMC (Call Option).
45 Section 16(h), DRA – Convertibility Feature.
46 Beginning on the thirty first (31st) day after the end of the third (3rd) year from Issue Date and shall expire sixty (60) days thereafter.
47 The CN was issued by Appellant VMC through its President & CEO, Arthur N. Aguilar and Senior Vice President, Abelardo E. Bugay. This was accepted by Appellee EWBC through its Vice Chairman, Edmundo A. Barcelon.
48 *Paragraph 1, CN* -FOR VALUE RECEIVED, VICTORIAS MILLING COMPANY, INC. a corporation duly organized and validly existing under the laws of the Republic of the Philippines (the "ISSUER") hereby unconditionally promises to pay EAST WEST BANKING CORPORATION (the "HOLDER") with principal office x x x on September 1, 2018, in immediately available funds, the principal amount of x x x (PhP 200,396,734.00) at the rate of Eight Percent (8%) per annum, subject to the terms and conditions provided hereinbelow.

> ***"Paragraph 5 -***
> **The Holder has the <u>right and option to convert this Note</u> into common shares of the Issuer <u>during the designated conversion periods</u> beginning on the 31st day after the end of the (3rd, 4th, 5th, 6th, and 7th year) from the Issue Date and shall expire sixty (60) days thereafter (the "1st/2nd/3rd/4th/5th Conversion Periods")** at an amount not exceeding the maximum available amounts for conversion provided for each conversion period. Any outstanding convertible note at the end of the 5th Conversion Period may be converted per year from the 8th year to the 14th year within a period beginning on the 31st day after the end of each succeeding year from the 5th Conversion Period and shall expire sixty (60) days thereafter, A Final Conversion Period, beginning on the 60th day before the end of the 15th year from Issue Date and expiring 30 days thereafter, shall be allowed for the conversion of any or all Notes which were not converted during the previous conversion periods.
>
> x x x x x x x x x
>
> ***Paragraph 8 -***
> **"The issuer shall have the <u>option to redeem this Note by paying the Holder in cash</u> an amount equivalent to the subscription price, plus all accrued interest** beginning at the end of the third **(3rd) year** from the Issue Date and ending on the last day of the fifteenth (15th) year from Issue Date (the "Final Redemption Date"). **The Issuer may exercise its option to redeem this Note <u>at any time prior to Final Redemption Date by sending written notice</u> thereof to the Holder, which notice, when so sent, <u>shall be deemed final and irrevocable</u>. Notwithstanding the foregoing, <u>the conversion of this Note into common shares of the Issuer at the option of the Holder during the conversion period shall prevail over the exercise by the Issuer of its option to redeem this Note.</u>"**

Stated otherwise, Appellant VMC has the right to redeem the issued CN by paying in cash to Appellee EWBC, the subscription price plus accrued interest, at any time beginning at the end of the third (3rd) year from the Issue Date (01 September 2003) and ending on the last day of the fifteenth (15th) year (01 September 2018) from Issue Date. Appellant VMC's right to redeem may be exercise by sending only a written notice to Appellee EWBC which shall be deemed final and irrevocable.

On the other hand, Appellee EWBC has the right to convert the issued CN only during designated conversion periods[49]. Indeed, as expressly above-provided, during the conversion periods, Appellee EWBC's right to convert the CN shall prevail over the Appellant VMC's right to redeem[50].

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[49] Section 16(h) of the DRA, paragraph 5 of the CN.
[50] Paragraph 8, last sentence of the CN.

In view of the above-discussed interpretation of the agreements executed by the parties, we now delve into SHP1's *Decision* which is subject of this appeal.

SHP1 was in error in ruling that Appellee EWBC's right to convert the CN is superior over Appellant VMC's right to redeem the said note based on the following:

First, The DRA and CN do not provide that Appellee EWBC is not obligated to accept payment by Appellant VMC. Conversely, it is clear in the DRA and CN that Appellee EWBC's right to convert the CN is limited only during conversion periods as provided in Section 16 (h) – Convertibility Feature of the DRA and paragraph 5 of the CN. It is also expressly provided in the said stipulations that the Appellee EWBC has the option to convert the CN but following a schedule which are specified in the DRA and CN as conversion periods. Hence, Appellee EWBC does not have the right to convert the CN outside of the conversion periods.

These stipulations are consistent with the fact that the CN is specifically designed as an alternative mode of payment for Appellant VMC's debts owning to Appellee EWBC. The convertibility feature of the CN serves as a security/guarantee that Appellant VMC will pay its debts. The CN's primary purpose is for Appellant VMC to pay its debts owning to Appellee EWBC as provided for in paragraph 5(b) of the former's ARP.

In the instant case, Appellant VMC on 24 February 2014 and 03 April 2014 notified Appellee EWBC that it will be paying/redeeming the issued CN. However, it was Appellee EWBC who refused to accept the payment of the same for the reason that it will be exercising its right to convert the CN.

But evaluating the surrounding circumstances, it can be evidently seen that Appellant VMC exerted its right to pay/redeem prior to and outside of the conversion period.[51]. Appellant VMC, aside from notifying in writing, even tendered the full amount of the CN as payment to Appellee EWBC. Moreover, it consigned the payment with the Rehabilitation Receiver.

Then again, Appellee EWBC refused to accept payment of the same because it opted to exercise its right to convert the CN. However, Appellee EWBC assertion of its right to convert was done outside of the designated conversion period. During that time, Appellee EWBC's right to convert cannot yet be exercised since the DRA and CN specifically provides that Appellee EWBC's right to convert the CN should be made during conversion periods which is a period beginning on the Thirty First (31^{st}) day after the end of the third (3^{rd}) year from Issue Date[52] and shall expire Sixty (60) days thereafter or from October 1, 2014 to November 29, 2014 (11^{th} year).. Hence, its

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[51] 11^{th} year from Issue Date, October 1 – November 29, 2014.

[52] 01 September 2003.

refusal to accept Appellee VMC's payment/redemption on 24 February 2014 and 03 April 2014 is without basis.

The SHP1 was mistaken to rely heavily on paragraph 8 of the CN to declare that Appellee EWBC's right to convert is superior over Appellant VMC right to redeem, to wit:

> "x x x Notwithstanding the foregoing, **the conversion of this Note** into common shares of the Issuer **at the option of the Holder** *(Appellee EWBC)* **<u>during the conversion period</u> shall prevail over the exercise by the Issuer** *(Appellant VMC)* **of its option to redeem** this Note."

As above-stated, while it is true that Appellee EWBC's right to convert shall prevail over Appellant VMC's right to redeem/pay but this is only available during the conversion periods. Thus, SHP1 was clearly mistaken to interpret that such right is superior at all times because the terms and conditions of the DRA and CN provides otherwise.

Second, the obligations of Appellant VMC, based on the above-discussed terms and conditions in the DRA and CN, are considered as an obligation with a period. The New Civil Code illustrates an obligation with a period as:

> "Article 1193. Obligations for whose fulfillment a day certain has been fixed, shall be demandable only when that day comes. Obligations with a resolutory period take effect at once, but terminate upon arrival of the day certain. A day certain is understood to be that which must necessarily come, although it may not be known when. If the uncertainty consists in whether the day will come or not, the obligation is conditional, and it shall be regulated by the rules of the preceding Section.
>
> x x x x x x x x x
>
> Article 1196. Whenever in an obligation a period is designated, it is presumed to have been established for the benefit of both the creditor and the debtor, unless from the tenor of the same or other circumstances it should appear that the period has been established in favor of one or of the other.

According to Manresa's classic definition, a term or period is an interval of time, which, exerting an influence on an obligation as a consequence if a juridical act, either suspends its demandability or produces its extinguishment. Hence, Obligations with a period may be defined as those whose demandability or extinguishment is subject to the expiration of a term or period[53]. A term or period may be classified as Suspensive (*ex die*) or Resolutory (*in diem*). **It is Suspensive when the obligation becomes demandable only upon the arrival of a day certain**; it is Resolutory when the obligation is demandable at once, although it is terminated upon arrival of a day certain[54].

If the term or period is suspensive, **the fulfillment or performance of the obligation is demandable only upon arrival of the day certain or the expiration of the term**. What is therefore suspended by the term is not the acquisition of the right or the effectivity of the obligation but merely its demandability. In other words, **the obligation itself becomes effective upon its constitution or establishment, but once the term or period expires it becomes demandable**. However, if the term or period is resolutory, the fulfillment or performance of the obligation is demandable at once, but it is extinguished or terminated upon arrival of the day certain or the expiration of the term[55].

In the instant case, there are two obligations imposed on Appellant VMC that were constituted in the DRA and CN, to wit: 1.) the obligation to pay/redeem the issued CN by paying the subscription price with interest; and 2.) the obligation to convert its common shares in favor of Appellee EWBC at the latter's choice only during conversion periods at an amount not exceeding the maximum available amount provided under Section 16(h) of the DRA.

Appellant VMC's obligation to pay/redeem the CN is demandable at any time beginning from the third (3rd) year from Issued Date and ending until fifteenth (15th) year from Issue Date[56]. Thus as above-discussed it is considered as an Obligation with a Suspensive Period because the fulfillment or performance of the obligation to pay is demandable starting on the third (3rd) year from Issue Date and ends in the fifteenth (15th) year from Issue Date.

On the other hand, Appellant VMC's obligation to convert its common shares in favor of Appellee EWBC is demandable only during conversion periods. As provided in Section 16(h) of the DRA and paragraph 5 of the CN, the conversion period begins on the 31st day after the end of the 3rd, 4th, 5th, 6th, and 7th year from Issue Date and shall expire sixty (60) days thereafter. This is considered also as an Obligation with a Suspensive Period because the demandability of the obligation to convert arises only upon arrival of day certain or in this case the designated conversion periods. Appellee EWBC has the right to convert the CN but it is not yet demandable until the arrival of the conversion periods.

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53 Comments and Jurisprudence on Obligations and Contracts, Desiderio P. Jurado, 11th Revised Edition, 2002, p.162 citing 8 Manresa, 5th Ed., Bk. 1, p. 140 citing 8 Manresa, 5th Ed. Bk. 1, p. 370.
54 Ibid, p. 141.
55 Ibid, p. 143.
56 Paragraph 8 of the CN.

Thus, Appellee EWBC may only exercise its right to convert only during designated conversion periods as provided under the DRA and CN. Therefore, Appellee may not demand its right to convert outside of the conversion periods since such obligation is one with a suspensive period.

Finally and in relation to Article 1196, it is worth mentioning that a rehabilitation proceeding is mainly intended for the benefit of a distressed corporation. In *Philippine National Bank, et al. vs. Honorable Court of Appeals, et al.*, the Supreme Court ruled that:

> "x x x is to enable the company to gain new lease on life and thereby allows creditors to be paid their claims from its earnings. **Rehabilitation contemplates a continuance of corporate life and activities in an effort to restore and reinstate the financially distressed corporation to its former position of successful operation and solvency.** This is in consonance with the State's objective to promote a wider and more meaningful equitable distribution of wealth to protect investments and the general public. It is precisely based on these principles that the SEC decided the petition for rehabilitation. x x x.[57]"

Moreover, in *Bank of Philippine Islands vs. Sarabia Manor Hotel Corporation*, the Supreme also ruled that:

> "Verily, the purpose of rehabilitation proceedings is to enable the company to gain a new lease on life **and thereby allow creditors to be paid their claims from its earnings**. Thus, rehabilitation shall be undertaken when it is shown that the continued operation of the corporation is economically more feasible and its creditors can recover, by way of the present value of payments projected in the plan, more, if the corporation continues as a going concern than if it is immediately liquidated.[58]"

In the instant case, Appellant VMC sought rehabilitation when it filed its *Petition for Declaration of State of a Suspension of Payments; Approval of a Rehabilitation Plan; and Appoinment of a Management Rehabilitation Committee.* Upon approval of its Rehabilitation Plan, Appellant VMC's debts with various creditors, including Appellee EWBC, was restructured in order to pay its outstanding loan obligations.

The very essence of a rehabilitation proceeding is for the corporation to gain a new lease on life and to allow it to recover from its distressed condition. Relative thereto, any ambiguities in the ARP, DRA and CN should be construed or interpreted in favor of the rehabilitation of Appellant VMC. A contrary construction or

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[57] 576 SCRA 537, 559.
[58] G.R. No. 175844, July 29, 2013.

interpretation of the ARP, DRA and CN would run counter to the very purpose of Appellant VMC's rehabilitation.

WHEREFORE, premises considered, the instant *Appeal* is hereby **GRANTED**. The Special Hearing Panel 1's *Order* dated 19 March 2015 is hereby **REVERSED AND SET ASIDE**. Thus, East West Banking Corporation's *Motion to Compel Victorias Milling Corporation (sic) to Allow EWBC to Exercise its Option for the Conversion of the Uncontroverted Convertible Note (CN)* filed with the Special Hearing Panel 1 is hereby **DENIED**.

SO ORDERED.

Mandaluyong City, Philippines; 11 August 2015.

TERESITA J. HERBOSA
Chairperson

ANTONIETA F. IBE
Commissioner

MANUEL HUBERTO B. GAITE
Commissioner

EPHYRO LUIS B. AMATONG*
Commissioner

Blas James G. Viterbo

BLAS JAMES G. VITERBO
Commissioner

* Onofficial business