Republic of the Philippines
Department of Finance
Securities and Exchange Commission
PICC Secretariat Building, PICC Complex, Pasay City

SAVINGS AND LOAN ASSOCIATION OF P&G PHILS. EMPLOYEES, INC. (PECA)
Appellant,

SEC En Banc Case No. 03-17-423
Re: Violation of Memorandum Circular No. 08, Series of 2009

COMPANY REGISTRATION AND MONITORING DEPARTMENT,
Appellee.

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DECISION

For the consideration of the En Banc is a **Memorandum of Appeal**[1] filed on 3 March 2017 by Appellant **SAVINGS AND LOAN ASSOCIATION OF P&G PHILS. EMPLOYEES, INC. (PECA)**, praying that the En Banc reverse the Letter-Orders of the Commission's **COMPANY REGISTRATION AND MONITORING DEPARTMENT (CRMD)**, dated 7 August 2015 and 22 January 2016 wherein CMRD imposed a Fine for ***material misstatement***[2] in PECA's 2013 Audited Financial Statements.

RELEVANT FACTS

PECA is a duly-registered **Corporation** (SEC Registration No. 0000039904), whose purpose[3] is the **"operation of a non-stock savings and loan association."** As with all corporations, PECA is obligated to submit its annual Audited Financial Statements (AFS) to the Commission. **Section 68 of the Securities Regulation Code** (SRC) authorizes the Commission to "make, amend, and rescind such accounting rules and regulations as may be necessary to carry out the provisions of this Code."

Furthermore, **Memorandum Circular No. 08, Series of 2009** authorizes the imposition of a Fine of P2,000 or **1/10 of 1% of the amount of misstatement**, whichever is higher[4] if a private corporation makes a "material misstatement" in its financial statements, defined generally as an "overstatement or understatement of income, asset, **liability**, or **equity**, that the Commission may consider material."[5] (Emphasis supplied) The allegedly misstated entry here is **P1,182,526,675** which is the total amount of **withdrawable capital contributions** of PECA members.

As a **Non-Stock Savings and Loan Association**, however, PECA falls under the regulatory supervision of the **Bangko Sentral ng Pilipinas (BSP)**. Section 22

[1] Dated 2 March 2017.
[2] Material overstatement of Liabilities, resulting in Material understatement of Members' Equity.
[3] 2nd Paragraph of the Amended Articles of Incorporation of PECA dated 11 January 2002.
[4] Number I (A) – Scale of Fines; Ordinary Corporations with no Secondary License.
[5] Number III (B)(6) – Test of Materiality; Other Misstatements.

("Regulatory Powers over Associations") of Republic Act No. 8367 aka the Revised Non-Stock Savings and Loan Association Act of 1997 provides that:

> Notwithstanding the provisions of Section 130 of Republic Act No. 7653, the power to regulate the operations of any Association by the [BSP's] Monetary Board shall continue and consist of the following: xxx
>
> (b) [R]egulating the operation and activities of Associations, which include[s], among others: xxx
>
> (3) [I]mposing a **uniform accounting system** and manner of keeping the accounts and records of Associations; **(Emphasis supplied)**
>
> xxx xxx xxx
>
> The Bangko Sentral shall have the power to enforce the laws, orders, instructions, rules and regulations promulgated by the [BSP's] Monetary Board applicable to [Non-Stock Savings and Loan] Associations xxx

The BSP also is specifically empowered to require the submission of Annual Reports showing "the amount and character of assets and liabilities" (Section 21 of R.A. 8367) and impose Penalties for the "**willful** making of false statement or misleading statement on a material fact" (Section 23[b] of R.A. 8367).

On **28 July 2014**, in its capacity as a Non-Stock Savings and Loan Association, PECA filed its Financial Audit Report (**FAR**) for the year 2013 with the BSP.

On **25 April 2014**, PECA also filed its Annual Financial Statements (**AFS**) for the year 2013 with the Commission. In both initial filings, PECA booked the ***withdrawable capital contributions*** of its members under ***liabilities***. This was allegedly[6] in accordance with Philippine Financial Reporting Standards (PFRS) and the definition of "financial liability" under Philippine Accounting Standard (PAS) 32 (effective 1 January 2009).

On **8 August 2014**, the BSP wrote a Letter ordering PECA to submit a revised FAR, essentially because under **BSP Circular No. 789** dated 28 February 2013, ***withdrawable capital contributions*** should be booked as ***members' equity***.

On **4 September 2014**, PECA submitted its **revised FAR** to the BSP, wherein it reclassified the **P1,182,526,675 withdrawable capital contributions** from ***liabilities*** to ***members' equity***.

On the same day, PECA submitted a **revised AFS** to the Commission, upon the same **reclassification** of withdrawable capital contributions.

On **15 September 2014**, the BSP wrote a Letter, acknowledging that PECA complied with the BSP's directive to reclassify its withdrawable capital contributions.

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[6] Paragraph 3.2 of PECA's Memorandum on Appeal.

On **7 August 2015**, the CRMD issued a Letter-Order imposing a Fine of **P1,185,526** (1/10 of 1% of **P1,182,526,675**) against PECA for material overstatement of Liabilities, resulting in material understatement of Members' Equity. In response to the PECA's claim that it was merely following BSP's directive, the CRMD stated that:

> The contention that the filing of the amended 2013 AFS was due to the directive of the BSP hence [PECA] did not violate MC 8 [series] of 2009 is not meritorious. In the first place, such directive of BSP would not have been issued had the classification of accounts in the original 2013 AFS of the subject corporation [been] correct.[7]

The CRMD stressed that the **Rule 68 of the [2006] Implementing Rules and Regulations (IRR) of the SRC** which deals with "Re-Issuance of Financial Statements" expressly provides that:

> (iii) An **amendment** or re-issuance of the financial statements **shall not exonerate the company** from the penalty that may be assessed by the Commission due to the **material** deficiency or **misstatement of the original financial statements.** (Emphasis supplied)[8]

The CRMD's Letter-Order likewise stated that the Commission's Office of the General Accountant (OGA),[9] in the latter's Memorandum dated 3 February 2015, confirmed that:

> The misstatement constitutes more than 10% of the Total Liabilities and Total Members' Equity xxx **[T]he amendment of the said AFS will not cure the defect in the original AFS[;] hence, [PECA] should be assessed with a penalty** for its violation of SRC Rule 68, as amended, based on SEC MC No. 8, Series of 2009.[10] (Emphasis supplied)

On **28 October 2015**, the PECA wrote to the CRMD, asking the Commission to reconsider the fine imposed. PECA claimed that its *reclassification* cannot be penalized as a *material misstatement* since it was merely obeying the regulating agency, the BSP.

On **22 January 2016**, the CRMD sent a Letter-Order reiterating the imposition of Fine and denying with finality the request for reconsideration, to wit:

> In view of the foregoing, we reiterate the denial of your request per our letter-reply dated 7 August 2015.
>
> Should you have any more contentions, the proper procedure is to appeal the same to the Commission En

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[7] Page 2 of CRMD Letter-Order dated 7 August 2015.
[8] Id.
[9] **Annex K** of PECA's Memorandum on Appeal.
[10] Id.

> Banc pursuant to Rule XI of the 2006 Rules of Procedure of the [SEC].[11]

In this regard, **Rule XI of the 2006 SEC Rules of Procedure** provides that:

> **Sec. 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.
>
> **Sec. 11-2. How Appeal is Taken.** – Appeal may be taken by serving upon the adverse party and filing with the Commission En Banc **<u>within fifteen (15) days from notice of Decision, Order or Ruling</u>**, a Notice of Appeal and a Memorandum on Appeal and paying the corresponding docket fee therefor xxx (Emphasis supplied)

On **3 March 2017**, PECA filed the instant Appeal to the Commission En Banc. In addition to its previous arguments, PECA argued that the OGA acquiesced that:

> Considering that the subject company is regulated by [the] Bangko Sentral ng Pilipinas, it is recommended that inquiry be made if clearance for the amendment of AFS is required from said agency.[12]

According to PECA, "It does not appear, however, that the Operating Department made any confirmation or inquiry with the BSP on the foregoing matter."[13]

Hence, this Appeal.

DISCUSSION

It must be mentioned at the outset that the instant Appeal was filed **<u>more than a year after</u>** the lapse of the 15-day reglamentary period. The procedural rules dictate that this appeal should not be given due course. However, this being an administrative proceeding, procedural rules may be relaxed, especially if there are compelling substantial arguments.

<u>The issue here is whether PECA's **reclassification** of withdrawable capital contributions from liabilities to members' equity, to comply with BSP rules, can be penalized as a **material misstatement** under the Commission's rules.</u> PECA argues that it is primarily governed by BSP, and that the BSP has already absolved PECA from material misstatement. BSP's exercise of discretion prevents the Commission from imposing a fine.

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[11] Page 2 of CRMD Letter-Order dated 22 January 2016.
[12] Supra note 9.
[13] Paragraph 5.4 of PECA's Memorandum on Appeal.

The appeal is impressed with merit.

The **Revised Non-Stock Savings and Loan Association Act of 1997**[14] makes it very clear that the regulatory body over such entities is the BSP. It is the appropriate government agency to require the submission of annual reports and to impose penalties.

PECA is a Non-Stock Savings and Loan Association. Even though it is also registered as a corporation with the Commission, it is primarily governed by the BSP. This includes discretion over reportorial requirements and penal provisions.

In fact, the OGA did not dispute that primary jurisdiction to make and enforce rules belongs to the BSP, and it also conceded that clearance for the reclassification must be sought by the CRMD from the BSP. **If the BSP has exercised its discretion on a certain matter, such as whether the *reclassification* would qualify as a *material misstatement*, the Commission must defer to the BSP's wisdom.**

In order to gauge whether the reclassification constitutes a punishable material misstatement, we must consult the BSP rule on material misstatements by a Non-Stock Savings and Loan Association. **Note that the BSP rule on material misstatement is different from the Commission's rule.** The term "willful" is very conspicuous in the BSP rules, to wit:

> The **willful** making of a false statement or misleading statement on a material fact to the Monetary Board or to the director of the department of the Bangko Sentral charged with the regulation of Associations or to his examiners shall be punished in accordance with Section 35 of Republic Act No. 7653.[15] (Emphasis supplied)

Absent willfulness, a false or misleading statement on a material fact would not be penalized by the BSP. **On the other hand, willfulness is irrelevant in the Commission's rules**, as long as there is an "overstatement or understatement of income, asset, ***liability***, or ***equity***, that the Commission may consider material."[16] Furthermore, under the Commission's rules, subsequent amendment does not absolve a corporation from liability for material misstatement. The Commission's rules thus focus on the *mere occurrence* of the misstatement and not its willfulness or *intent*. **This is because material misstatement under the Securities Regulation Code is a *mala prohibita* offense.**

Here, the BSP applied its criteria of *willful* material misstatement and decided not to impose a fine. **The BSP sent PECA a letter, directing the reclassification of withdrawable capital contributions from *liabilities* to *members' equity* in order to abide by rules likewise issued by the BSP**. When PECA complied with BSP's letter and performed the reclassification, the BSP duly acknowledged the correction. The BSP did not begrudge that PECA *should have* performed the correct classification to begin with (which is the rationale for the Commission's stricter rule). **Indeed, the BSP could have imposed fines if so warranted, but it did not do so.** The Commission has to defer to the wisdom of the governing agency.

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[14] Sections 21, 22, 23.
[15] Section 23(b) of the Revised Non-Stock Savings and Loan Association Act of 1997.
[16] Supra note 5.

Therefore, when CRMD applied the Commission's criteria for material misstatement and imposed a fine, it erroneously substituted the BSP's judgment with its own. At the very least, the CRMD should have taken OGA's suggestion to have prior consultation with the BSP as to the basis and/or effect of the latter's decision not to penalize PECA, but it failed to do so. Stated otherwise, the CRMD exceeded its jurisdiction.

WHEREFORE, premises considered, the Appeal is hereby **GRANTED**. The Letter-Orders of the CRMD dated 7 August 2015 and 22 January 2016, imposing a Fine for ***material misstatement***[17] in PECA's 2013 Audited Financial Statements, are hereby **REVERSED**.

SO ORDERED.

Pasay City, Philippines; 14 September 2017.

TERESITA J. HERBOSA
Chairperson

please see separate concurring opinion

ANTONIETA F. IBE *
Commissioner

**** EPHYRO LUIS B. AMATONG**
Commissioner

BLAS JAMES G. VITERBO
Commissioner

EMILIO B. AQUINO
Commissioner

*On Leave
** Separate concuring opinion to follow.

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[17] Supra note 2.