OFFICE OF THE GENERAL COUNSEL

11 October 2024

SEC-OGC Opinion No. 24-30
Re: Exemption from Securities Registration;
Cooperatives

TEKTON ENTRE MULTIPURPOSE COOPERATIVE
Bathan Bldg., Jereza Street Cor. Burgos,
Brgy San Roque.,
Cebu City, Philippines

Attention: Dr. Francisco B. Noob, DMD

Dear Dr. Noob,

This is in connection to your letter[1] requesting for an opinion regarding securities issued by cooperatives.

In your letter, you mentioned that **Tekton Entre Multipurpose Cooperative ("Tekton")** is a duly registered cooperative under the Cooperative Development Authority (CDA) established as part of the social development programs of *Couples for Christ Global Mission Foundation* in the Philippines. It is a manpower service cooperative engaged in job-contracting activities duly licensed under the Department of Labor and Employment (DOLE).

You stated that Tekton has, as of the date of your letter, already over 7,000 plus member-employees, having nationwide operations in areas of agriculture, restaurant, solar panel distribution and installation, and real estate development.

Due to Tekton's plan of developing raw lands with various lot owners to convert them into **Co**mmercial-**Res**idential-**Ho**tel or "**CoResTel**", the Committee on Membership of Tekton plans to engage in various forms of advertisements and marketing activities like newspaper, magazines, brochures, tarpaulins, mall exhibits, seminars, as well as social media platforms such as Facebook, Youtube, etc. in order to attract more members and obtain more capital build-up.

You further provided the following facts:

TEKTON's Operation	
Type of Cooperative	Multipurpose cooperative including job contracting, credit/ lending, solar distribution and installation, travel and tours, real estate, etc.
Date Registered	December 8, 2009
Capitalization	Php 50,000,000.00 currently processing to increase Php 480,000,000.00
Scope of Membership	Nationwide per Amended Articles and By-laws
Coverage in Recruitment of Investors	Nationwide but Non-members shall attend PMES to become members before signing Subscription Agreement

[1] Letter dated 30 July 2020 addressed to Director Lindaeza Rojero-Gavino of SEC-Cebu Extension Office.

Proof of Agreement	Subscription Agreement to buy common shares thru continuous capital build up
Promise of Return	Patronage refund, Interest on Share Capital, Dividend Income of all net revenues of Tekton and free 7-day staycation in the hotel once buildings are completed.
Pre-Membership Education Seminar	Conduct PMES to non-members to prequalify them to become member.
Manner of Promoting and Advertising Cooperative	Plans to use brochures, tarpaulins, Facebook, Youtube, Messenger, Viber and other online engines.
Manner of Recruitment	Committee on Membership and Committee on Education and Training will take the lead in the recruitment of members.
Award to who can recruit	Plans to give commissions and incentives but if not allowed, to give honorarium or per diem to those who help in the PMES for the time and work hours spent.

Given the foregoing, you seek clarification on the following issues:

1. "Shall Tekton apply from the Securities and Exchange Commission (SEC) a secondary license for the issuance of shares to its (sic) 7,000 members of the cooperative and prospective members of the cooperative, since they are planning to increase their membership to around 150,000 members to build up capital for Real Estate Development projects and other business segments, and considering Article 61(8) of Republic Act (R.A.) No. 9520 or the Philippine Cooperative Code of 2008?"

2. "If the cooperative is exempted from the provisions of the Securities Act, shall the cooperative be required to apply for exemption under Sec. 10.3 of the Securities Regulation Code (SRC)[2]? "

3. "With respect to acquiring and attracting members of the cooperative, shall SEC require the Membership Committee of Tekton to apply (sic) a license as security broker from SEC?"

"Securities" under the SRC vis-à-vis "Shares" under R.A. No. 9520

Securities under Section 3.1 of the SRC is defined as:

> "Section 3. **Definition of Terms** – 3.1 "Securities" are shares, participation or interest in a corporation or in a commercial enterprise or profit-making venture and evidenced by a certificate, contract, instrument, whether written or electronic in character. It includes:
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> (a) **Shares of stock**, bonds, debentures, notes, evidences of indebtedness, asset backed securities;
> (b) Investment contracts, certificates of interest or participation in a profit sharing agreement, certificates of deposit for a future subscription;
> (c) Fractional undivided interests in oil, gas, or other mineral rights;

[2] *"10.3 Any person applying for an exemption under this Section, **shall file with the Commission a notice** identifying the exemption relied upon on such form and at such time as the Commission by rule may prescribe and with such notice **shall pay to the Commission a fee equivalent to one-tenth (1/10) of one percent (1%) of the maximum aggregate price or issued value of the securities."***

(d) Derivatives like option and warrants;
(e) Certificates of assignments, certificates of participation, trust certificates, voting trust certificates or similar instruments;
(f) Proprietary or non-proprietary membership certificates in corporations; and
(g) Other instruments as may in the future be determined by the Commission." *(emphasis, ours)*

In connection thereto, Section 8 of the SRC provides:

"Section 8. **Requirement of Registration of Securities.** — 8.1. Securities shall not be sold or offered for sale or distribution within the Philippines, without a registration statement duly filed with and approved by the Commission. Prior to such sale, information on the securities, in such form and with such substance as the Commission may prescribe, shall be made available to each prospective purchaser. xxx"

On the other hand, R.A. No. 9520 defines ***"shares"*** as:

"Article 76. *Shares*.- **The term "share" refers to a unit of capital in a primary cooperative** the par value of which may be fixed to any figure not more than One thousand pesos (P1,000.00). The share of capital of a cooperative is the money paid or required to be paid for the operations of the cooperative. The method for **the issuance of share certificates** shall prescribed in its bylaws." *(emphasis, ours)*

Based on the above-mentioned provisions, the shares being issued by cooperatives are within the ambit of the definition of securities. However, Tekton points out Section 61(8) of R.A. No. 9520, which reads:

"Article 61. *Tax and Other Exemptions.*

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(8) Any security issued by cooperatives **shall be exempt** from the provisions of the Securities Act **provided such security shall not be speculative**."

By the clear letter and spirit of R.A. No. 9520, securities issued by a cooperative are generally exempt from the coverage of the SRC, except when they are speculative, in which case, the SRC shall already apply.

Section 1 of Act No. 2581[3] defines speculative securities, to wit:

Section 1. Terms defined. — The term "securities" as used in this Act shall be taken to mean stock certificates, shares, bonds, debentures, certificates of participation, contracts, contracts or bonds for the sale and conveyance of lands on deferred payments or on the installment plan, or other instruments in the nature thereof, by whatsoever name known or called. The term **"speculative securities"** as used in this Act shall be deemed to mean and include:

(a) All securities to promote or induce the sale of which profit, gain, or advantage unusual in the ordinary course of legitimate business is in any way advertised or promised;

(b) All securities the value of which materially depends upon proposed or promised future promotion or development rather than on present tangible assets and conditions;

(c) All securities for promoting the sale of which a commission of more than five per cent is offered or paid;

(d) The securities of any enterprise or corporation which has included, or proposes to include in its assets as a material part thereof patents, formulae, good-will, promotion or other intangible assets, or which has issued or proposes to issue a material part of its securities in payment for patents, formulae, good-will, promotion or other intangible assets.

[3] Act No. 2581, AN ACT TO REGULATE THE SALE OF CERTAIN CORPORATION SHARES, STOCKS, BONDS AND OTHER SECURITIES or the Blue Sky Law, February 4, 1916.

In the case of *People v. Fernandez*[4], the Court held that the certificates of membership issued by the Philippine Mutual Cooperative Society, Inc., are truly speculative securities within the meaning of Act No. 2581, to wit:

> "First. In order to encourage and induce their sale, profit unusual in the ordinary course of business has been advertised or promised, for through the payment of the sum of P5 by a member appertaining to class O, or that of P2.50 by a member belonging to class S, each will receive profits of P40 and P20, respectively, which represent the fabulous and extraordinary gain of 800 per cent.
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> Second. The speculative character of said certificates is also shown by the fact that such profit or advantage of 800 per cent does not depend upon the actual tangible assets or conditions of the corporation, but upon its growth and development which would be attained through the admission of new groups of 16 or 12 members so that each original member could receive the benefit aids of P40 or P20, as the case may be. Therefore, if there were no enrollment of 16 or 12 new members, according to the class, a member of class O or class S would not receive the corresponding benefit aid of P40 or P20, respectively.
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> Third. Another proof of their speculative nature is that even if a member of class O or class S should be able to secure a group of 16 or 12 new members, as the case may be, this fact would not necessarily entitle him to receive immediately the benefit aid of P40 or P20, respectively, for according to the by-laws of the corporation, he would have to wait for his turn before he could receive his benefit aid. And it is possible that his turn may never come because notwithstanding the admission of 16 or 12 members, according to the class, there may be no funds with which to pay his benefit aid, for before the coming of his turn, the funds of the corporation might have been exhausted by the payment of the dues of the old members in accordance with the strict rotation, while no new members may have been admitted in the meantime.
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> Fourth. The certificates of membership in question also come within the purview of paragraph (c) of section 1 of Act No. 2581 because to promote their sale, the corporation has offered and paid a commission of 10 per cent which, though later on reduced to 5 per cent, was in fact more than 5 per cent because the corporation has paid another 5 per cent for traveling expenses.
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> Fifth. The speculative character of the membership certificates issued by the corporation is also shown by the fact that when a member, whether belonging to class O or to class S, has not received his benefit aid after two years from the date of his enrollment, he cannot expect anything more than the refund of the dues paid by him plus 25 per cent of the same. But it is possible, as the by-laws of the corporation themselves provide, that there are no funds with which to reimburse the member or members, who have not been able to collect any benefit aid, the dues paid by them. To avoid such an eventuality, it is provided that the corporation hold public contests and benefit performances, the net proceeds of which will be applied to the payment of benefit aids. It may, however, happen that, even by these means, the corporation will not be able to raise the necessary funds to pay the members, who ask for reimbursement of their dues, as would undoubtedly occur should no new members enroll in the corporation."

The concept of speculative securities was further elucidated in Section 2(b) of Commonwealth Act No. 83[5] or the Securities Act, with the addition of other circumstances under items 4 and 6, to wit:

> "(b) **"Speculative securities"** shall mean and include:
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> 1. All securities to promote or induce the sale of which profit, gain, or advantage unusual in the ordinary course of legitimate business is in any way advertised or promised;
>
> 2. All securities the value of which materially depends upon proposed or promised future promotion or development rather than on present tangible assets and conditions;
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> 3. All securities for promoting the sale of which a commission of more than five *per centum* is offered or paid;
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> 4. All securities into the value of which the elements of chance or hazard or speculative profit or possible loss equals or predominates over the elements of reasonable certainty or safety of investment;

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[4] People v. Fernandez, G.R. No. 45655, 15 June 1938, 65 Phil 675-684.

[5] Securities Act, Commonwealth Act No. 83, October 26, 1936.

5. The securities of any enterprise or corporation which has included, or proposes to include, in its assets, as a material part thereof, patents, formulae, good-will, promotion or other intangible assets, or which has issued or proposes to issue a material part of its securities in payment for patents, formulae, good-will, promotion or other intangible assets; and

6. The securities of any enterprise engaged in the business of promoting, exploring, developing, exploiting or operating mineral properties and/or mineral rights: *Provided, however,* That the following class of securities shall not be deemed to be speculative securities:

(1) Securities issued by a person owning a property, business or industry which has been in continuous operation not less than three years and which has shown during a period of not less than two years next prior to the close of its last fiscal year preceding the offering of such securities, average annual net earnings, after deducting all prior charges not including the charges upon securities to be retired out of the proceeds of sale, as follows:

(a) In the case of interest-bearing securities, not less than one and one-half times the annual interest charged thereon and upon all other outstanding interest-bearing obligations of equal rank;

(b) In the case of preferred stock, not less than one and one-half times the annual dividend requirements on such preferred stock and on all other outstanding stock of equal rank;

(c) In the case of common stock, not less than five *per centum* upon all outstanding common stock of equal rank together with the amount of common stock then offered for sale reckoned upon the price at which such stock is then offered for sale or sold.

The ownership by a person of more than fifty *per centum* of the outstanding voting stock of a corporation shall be construed as the proportionate ownership of the property, business or industry of such corporation, and shall permit the inclusion of the earnings of such corporation applicable to the payment of dividends upon the stock so owned in the earnings of the person issuing the securities sought to be registered."

Based from the foregoing, the presence of any of the following circumstances renders the securities issued speculative:

1. Issuance is intended to encourage and induce their sale, profit, gain, or advantage unusual in the ordinary course of legitimate business has been advertised or promised.
2. The value of securities does not materially depend upon the actual tangible assets or conditions of the corporation, but upon its growth and development which would be attained through the admission of new members so that each original member could receive the benefit aids.
3. To promote their sale, the cooperative has offered or paid a commission of more than five percent (5%).
4. The cooperative will not be able to raise the necessary funds to pay the members, who ask for reimbursement of their dues, as would undoubtedly occur should no new members enroll in the corporation.
5. Those the value of which materially depends on proposed or promised future promotion or development, rather than on present tangible assets or conditions.
6. Investment contract such as certificates will be issued in consideration of cash and services entitling the holder to share in the profits of the business.
7. Those whose value depends on elements of chance, risk, speculative profit, or if the potential loss outweighs the factors of reasonable certainty or safe investment.
8. Those of any enterprise engaged in the business of promoting, exploring, developing, exploiting, or operating mineral properties and/ or mineral rights.

From the limited facts you have given, a few are relevant. Anent the promise of return, the *patronage refund, interest on share capital, dividend income of all net revenues of Tekton and free 7-day staycation in the hotel,* are not unusual and therefore not characteristic of a speculative security since they appear to be the standard benefits of members in a cooperative.[6] With regard to the award to be given to those who can recruit members, the sale of shares of Tekton may be considered speculative if Tekton will offer or pay a commission of more than five percent (5%) to those who promote such sale. As to the mode of advertisement and marketing activities to attract more members, the same is not considered as speculative provided that such promotion or marketing: 1) will not include an advertisement or promise of a profit, gain, or advantage unusual in the ordinary course of legitimate business; 2) will not offer or entitle the promoter to a commission of more than five percent (5%); and 3) will not show that the shares promoted derive their value merely or primarily from elements of chance or future promotion.

Thus, to answer your first query, for as long as no characteristic of a speculative security is present, the shares of Tekton shall be exempt from the SRC.

Application for Confirmation or Declaration of Exemption under Section 10.3 of the SRC

As to your second query, Section 10.3 of the SRC provides:

> "10.3. Any person applying for an exemption under this Section, shall file with the Commission a notice identifying the exemption relied upon on such form and at such time as the Commission by rule may prescribe and with such notice shall pay to the Commission fee equivalent to one-tenth (1/10) of one percent (1%) of the maximum value aggregate price or issued value of the securities."

In *SEC-OGC Opinion No. 13-13*, the Commission opined that unless a confirmation of the availability of an exemption is applied for, any person claiming [an] exemption under Section 10 has the burden, if challenged, to establish that the exemption is available and the Commission may challenge such exemption at any time. This means that although an application for confirmation is optional, a party may avail of such confirmation to defeat future challenge from the Commission.[7]

In sum, since there is already an applicable or available exemption, an application for confirmation of exemption under Section 10.3 is merely optional, for purposes of compliance under the SRC. But in order to avail the benefit of barring future challenges from the Commission, a party may opt to file such application for confirmation of exemption.

Registration of Brokers

As to your third query, of significance is Section 28 of the SRC which provides:

> "Section 28. Registration of Brokers, Dealers, Salesmen and Associated Persons. —
>
> 28.1. No person shall engage in the business of buying or selling securities in the Philippines as a broker or dealer, or act as a salesman, or an associated person of any broker or dealer unless registered as such with the Commission.
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> 28.2. No registered broker or dealer shall employ any salesman or any associated person, and no issuer shall employ any salesman, who is not registered as such with the Commission."

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The above-provisions must be read and interpreted in relation to Sections 8 and 10 of the SRC.

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[6] See Articles 7 and 87 of R.A. No. 9520.

[7] SEC-OGC Opinion No. 13-13 addressed to Mr. Jeric Hechanova dated 5 December 2013.

Consequently, if the shares issued by Tekton are exempted from the coverage of the SRC pursuant to Article 61(8) of R.A. No. 9520, then there is no need for the Committee Members of Tekton to apply for license as security broker or salesmen under Section 28 of the SRC.

It shall be understood that the foregoing opinion is rendered solely on the basis of the facts, circumstances and documents disclosed/submitted, and should be considered relevant solely to the particular issue raised therein. It shall not be used in the nature of a standing rule binding upon the Commission in other cases or upon the courts whether of similar or dissimilar circumstances. If upon investigation, it will be disclosed that the facts relied upon are different, this opinion shall be rendered null and void.[8]

Please be guided accordingly.

Respectfully yours,

ROMUALD C. PADILLA
General Counsel

[8] Paragraph 7, SEC Memorandum Circular No. 15, Series of 2003.

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