

**RURAL BANK OF LUCENA, INC., ET AL., PLAINTIFFS AND
APPELLANTS, VS. CENTRAL BANK OF THE PHILIPPINES, ET AL.,
DEFENDANTS AND APPELLANTS RED V COCONUT PRODUCTS LTD.,
INTERVENOR.**

G.R. No. L-19621. November 29, 1969

Ponente: DIZON, J.

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DIZON, J.:

Separate appeals taken by the Central Bank of the Philippines - hereinafter referred to as Central Bank - and the Rural Bank of Lucena, Inc. - hereinafter referred to as Lucena - from the decision of the Court of First Instance of Manila in Civil Case No. 47345 entitled "Rural Bank of Lucena, Inc. et al. vs. Central Bank of the Philippines, et al." enjoining the enforcement of Resolution No. 928 of the Monetary Board of the Central: Bank and sentencing the latter to pay Lucena the sum of P5,000.00 as damages, and the costs.

Lucena was incorporated under the Rural Banks' Act (Republic Act No. 720) with a paid-up capital of P60,000.00 later increased to P500,000.00 - and a capital assistance' of P100,000.00 in preferred stock from the Republic of the Philippines.

On January 14, 1959, the Rural Bank of San Pablo complained to the Central Bank that Lucena was operating a branch office in San Pablo City without authority from the Monetary Board. This caused the Governor of the Central Bank to send Mr. Celso S. Bate, Assistant to the Superintendent of Banks, to examine the affairs of Lucena. On February 11, 1959, Mr. Bate submitted his report find-ing, among other things, (1) that Lucena had been operating a branch office in San Pablo without proper authority; that it received savings accounts in spite of authority only to service current accounts and sales of drafts; cash deposits were received only by a mere helper; that it had extended loans up to the amount of P180,000.00 to 23 borrowers whose whereabouts could not be located and were probably either ineligible as borrowers or fictitious persons. In a second progress report submitted on February 23, 1959, said examiner charged:

“x x x x x x x x xxx that (1) the President-Manager of the plain-tiff Rural Bank has sole power to approve loans; (2) the credit standing and integrity of the President and members of the Boards of Directors of the plaintiff Rural Bank were not considered when certificate of authority was issued; (3) the employees handling cash and cash deposits were not bonded; (4) no punitive or disciplinary action has been taken against Rural Bank for extending anomalous loans or credits to ineligible borrowers; no adequate steps were taken to press collec-tion of loans to ineligible and/or non-existent borrowers; (6) irregularities and violations com-mitted by plaintiff Rural Bank were not brought to the attention of the Monetary Board; (7) the Department of Loans and Credit intervened in ap-ointment and separation of bank personnel; (8) the Department of Loans and Credit and Rural Banks Administration encouraged the illegal ope-ration of the Rural Bank 'Extension Office' in San Pablo City; (9) the Department of Loans and Credit and Rural Banks Administration has not exerted any effort to stop misleading and erron-eous advertisements of the plaintiff Rural Bank; and (10) that:

'a) the Management of the Rural Bank of Lucena is allegedly allergic to bank examination. In several instances,

Mr. Jose V. Perez, President-Manager of said bank, had displayed hostility and even threatened examiners pre-sently assigned thereat.

'b) Mr. Jose V. Perez, President-Manager of the Rural Bank of Lucena, allegedly has had highly questionable business transactions in connection with the infamous surplus property and immigration scandals.

'c) The Rural Bank of Lucena has flagrantly violated banking laws and Central Bank rules and regulations as a result of irresponsible and anomalous banking operations. This is especially true with regards to its lending operations and the handling of current accounts on which interest and/or premium appears to have been paid.

'd) The Rural Bank of Lucena is il-legally transacting business beyond its authorized territory of operation which is limited only to fifteen (15) towns in Quezon, Sariaya, Candelaria, Dolores, Ta-yabas, Lucban, Sampaloc, Mauban, Padre Burgos, Agdangan, Atimonan, Gumaca, Lopez, Cabuag, Tagkawayan and Pagbilao.' (Par. .7 [b]2, Partial Stipulation of Facts, p. 7 folder 1 of exhs.)"

On the same date (February 23, 1959) Bate submitted to the Governor of the Central Bank a specification of charges against the Director and Assistant Director of the Department of Rural Banks of the Central Bank as follows:

"(1) The Director and Assistant Director of the Department of Loans and Credit and Rural Banks Administration Did not Take Positive Steps to Stop, In Fact the Director Virtually Tolerated, the Illegal Operations of the 'Extension Office of the Rural Bank of Lucena in San Pablo City.

x x x x

"(2) The Director of the Rural Banks Administration Failed to Take Punitive or Disciplinary Action Against the Rural Bank of Lucena for Extending Anomalous Loans to Non-Existent or Ineligible Borrowers.

x x x x

"(3) The Director of the Rural Banks Administration Continued to Recom-mend Approval of the Various Loans and Capital Assistance Applied for by the Rural Bank of Lucena In Spite of the abovementioned Violations.

x x x x

"(4) The Director of the Rural Banks Administration Misrepresented the True Condition of the Management and Operation of the Rural Bank of Lucena in His Reports to the Monetary Board.

x x x x

"(5) The Director of Rural Banks Adminis-tration Failed to See to it that all the Personnel of the Rural Bank of Lucena Handling Cash and Other Account-abilities are Bonded; and

x x x x

"(6) The Director of the Rural Banks Admi-nistration Failed to Disclose in His Memorandum to the Monetary Board Re-lative to the Request of the ACCFA for an Additional Loan of P15,000.00 Mate-rial and Valuable Information on the Financial Condition of Said Institution.,. (Par. 7 [b]2, Partial Stipulation of Facts. p. 7. folder 1 of exhs.)"

Subsequently, another examination was conducted by Mr. Jose S. Martinez, then assistant superintendent of banks, who submitted a report to the Governor of the Central Bank enumerating therein a series of violations and irregularities committed by Lucena.

Acting on the reports of Messrs. Bate and Martinez, the Governor of the Central Bank issued on June 12, 1959 a memorandum to the Monetary Board providing for the steps to be taken "to prevent the Bank's (Lucena) condition from deteriorating" and also requiring Director Augusto F. Espiritu, of the Department of Rural Banks, to explain within seventy-two hours why he should not be suspended and investigated on the basis of the findings made against him. On June 16 of the same year the Monetary Board adopted Resolution No. 829 referring "back to the management the subject report on the special examination of the Rural Bank of Lucena, Inc., Lucena, Quezon, and the memorandum on the preliminary measures taken by the management incident thereto, with the request that the management analyze further the report and give the officials of the Central Bank charged in said report as having committed the irregularities pointed therein, a chance to explain their side in accordance with the pertinent rules and regulations of the Bureau of Civil Service".

Meanwhile, Messrs. Vicente Nacianceno and Diosdado Portugal, supervising bank examiner and senior bank examiner of the Department of Supervision and Examination of the Central Bank, respectively, were assigned to Lucena to assist and/or supervise its management.

On July 2, 1959, the Deputy Governor of the Central Bank wrote a letter to the President of Lucena calling his attention to several or repeated transactions which had been previously questioned, and directing him to remedy them; otherwise a more drastic action would be taken.

On July 29 of the same year Nacianceno and Portugal submitted their report listing therein the repeated irregularities committed by Lucena and recommending that its management be placed in more capable hands; that examiners of the Department of Rural Banks be detailed as Lucena's advisers, and that the matter of illegal practices be referred to the Department of Rural Banks for appropriate legal action.

Other examiners were sent subsequently, their reports always corroborating the findings of former examiners on them illegal practices of Lucena.

On April 6, 1960 Sixto de la Costa and Atty. Jose W. Diokno, Chairman of the Board of Directors of Lucena and counsel, respectively, wrote a letter to the Monetary Board requesting that action be taken to check and counter-act attempts made by the NBI to discredit Lucena by press releases. In reply thereto, the Governor of the Central Bank informed Lucena that the Central Bank was not the source of said publications. On May 23, 1960, the Board of Directors of Lucena wrote the Central Bank requesting that "before deliberating on any reports that may have been or may be submitted as a result of the many investigations and examinations, the Lucena Rural Bank, Inc. be furnished with copies thereof and permitted to submit its replies thereto, as well as given an opportunity to address the Monetary Board, through its Chairman of the Board, its President and/or its Counsel", and "that no publicity what-soever shall be given to the investigations heretofore conducted or examinations that may hereinafter be conducted of the Lucena Rural Bank; and, that, for any violation of these instructions, the heads of the said departments and office shall be held responsible".

On October 17, 1960, the Department of Rural Banks of the Central Bank sent a team of examiners to conduct an examination of the accounts and operations of Lucena. On November 25 of the same year, Lucena complained to the Monetary Board about certain acts of the examiners and asked for an opportunity to appear before it in the presence of the head of the examiners and proper officials of the Department of Rural Banks. For various reasons, however, the aforesaid team of examiners discontinued their examination of Lucena and returned to their post in Manila on December 20, 1960.

On February 21, 1961, following a conference with the Director of the Department of Rural Banks and the Governor of the Central Bank, counsel for Lucena wrote a letter to the Monetary Board informing the latter that an understanding had been reached by them concerning the examination of the loan portfolio and the financial

condition of Lucena. On March 18, 1961, the examination was resumed in accordance with the said "understanding" until May 16 when three examiners were allegedly manhandled by the guards of the Pre-sident-Manager of Lucena, which led to the filing of criminal cases for grave coercion and serious oral defa-mation against the latter. In turn, said examiners were charged with slander by deed and slight physical injuries.

Pursuant to a memorandum of Director Eugenio, the Monetary Board, on June 2, 1961, adopted Resolution 887, requesting "the management to invite the representatives of the Rural Bank of Lucena, Inc. to appear before the Monetary Board in connection with the report of the Di-rector, Department of Rural Banks, on certain practices of the said rural bank which would result in probable losses to its depositors". In a letter dated June 3, 1961, addressed to Mr. Sixto de la Costa, Chairman of the Board of Directors, the Monetary Board requested the members of the board of Lucena to appear at a hearing before it at 3:00 p.m. on June 9, 1961. On the same date counsel for Lucena wrote the Governor accepting the invi-tation but requested that it be furnished at least three days before the scheduled hearing on June 9, 1961 "with full particulars of the alleged unsafe banking practices, gross violations of the law, and serious irregularities, in the grant of loans including the existence of fictitious and padded loans' which are referred to in your letter". In compliance with this request, the Governor, on June 6, 1961, sent him the following bill of particulars, with attached schedules, regarding the preliminary findings in the examination of Lucena:

- "1. In the books of the Rural Bank are loans which have been totally denied by the borrowers (Schedule A).
- "2. In the books of the Rural Bank are loans where the amounts have been denied by borrowers (Schedule B).
- "3. Real estate securities were grossly misdescribed in the credit reports and in the mortgage documents to justify many loans granted by the Rural Bank.
- "4. The Bank has granted loans to in-dividuals and corporations who are not eligible as borrowers of a rural bank under Section 5 of Republic Act No. 720, as amended.
- "5. Upon inspection by fieldmen of the Department of Rural Banks, collaterals reportedly mortgaged to the Rural Bank were found to be non-existent.
- "6. The Bank has been chronically deficient in its available reserve against deposit liabilities.
- "7. The Rural Bank of Lucena has been sell-ing domestic drafts without sufficient covering funds with depository bank.
- "8. Certain obvious expenses of the Rural Bank have not been recorded in the books of the Rural Bank." (Exh. 98-Stipulation, pp. 177-178, folder 4 of exh; Par. 23 (b) Partial Stipulation of Facts, p. 16, folder 1 of exh.)

On the same date, Lucena's counsel wrote the Governor for additional data in connection with certain items among the bill of particulars to which the latter obliged in a letter dated June 7, 1961.

At the meeting held on June 9, 1961, the Chairman of the Board of Directors of Lucena and its counsel appeared. As a result of said proceedings, the Monetary Board adopted Resolution No. 924 requesting the Director of the Department of Rural Banks and the Lucena examiners, to sit with the representatives of the bank and indicate to the latter the, findings embodied in the preliminary report dated June 8, 1961 of the aforementioned Director relative to the exami-nation of the bank conducted on March 18, 1961.

In compliance with the aforesaid resolution, representa-tives of Lucena met with Director Eugenio on June 10, 1961, but nothing was accomplished because Director Eugenio terminated the meeting due to counsel for Lucena's remark that it was not a fair hearing. Two days later, Director Eugenio submitted his report on the

conference with the representatives of Lucena expressing the view that the latter had been resorting to delaying tactics to be able to gather false statements to counteract signed statements gathered by the, examiners, and recommending that "immediate action be taken on the recommendations contained in our Memorandum of June 6, 1961 in regards to our preliminary findings in the discontinued examination of the Rural Bank of Lucena, Inc.". On June 12, 1961, the Governor submitted a memorandum to the Monetary Board on the chronic reserve deficiencies of Lucena and recommending that the Bank's lending operations be immediately suspended for persistent violation of the law, and the taking of appropriate legal actions against its officers responsible for said violations.

On June 13, 1961, the Monetary Board held a meeting at which the Chairman of the Board of Directors of Lucena and its counsel appeared on its behalf, the former having had the opportunity to state fully the side of Lucena. As a result thereof, the Monetary Board adopted the questioned resolution No. 928, of which Lucena was officially notified on June 21, 1961. Before the latter date, or more specifically on June 16, 1961, Lucena had addressed another letter to the Monetary Board requesting that certain steps be taken to prevent a further run on the bank and praying that "the Bank be given a due hearing before any action be taken against the Bank".

Meanwhile, the Chairman of the Board of Directors of Lucena received a letter from the Governor of the Central Bank asking him to convene a stockholders' meeting on Tuesday, June 20, 1961, at 10:00 a.m. to discuss important matters relating to the affairs of Lucena. Pursuant thereto, a stockholders' meeting was called to be held at Manila instead of at Lucena and the Governor was notified of the place of said meeting on June 17, 1961. The aforesaid meeting was held as scheduled with all the members of the Board of Directors of Lucena present.

On the same date of the meeting on June 20, 1961, however, a team consisting of personnel from the Department of Rural Banks and other departments of the Central Bank, as well as from the Department of Justice, National Bureau of Investigation, and Philippine Constabulary, went to Lucena to deliver the letter dated June 16, 1961 quoting Resolution No. 928 mentioned heretofore, and immediately proceeded to implement the same.

The following day, June 21, 1961, the Manila Times carried the following headline story on Lucena: "BANK TOLD TO SUSPEND OPERATION", and in the afternoon of the same day the "Daily Mirror" published the following headline on its front page: "CHARGES TO FOLLOW CLOSURE OF BANK".

On June 22, 1961, Lucena, through its board of Directors, filed the present complaint for injunction with damages against the Central Bank of the Philippines, the Secretary of Finance, the Monetary Board of the Central Bank and its Governor, and the Director of the Department of Rural Banks of the Central Bank of the Philippines to desist them from carrying out Resolution No. 928 of the Monetary Board of the Central Bank; from causing any publication concerning the affairs of Lucena, and to condemn the defendants to pay damages.

Lucena claims that Resolution 928 of the Monetary Board is illegal because (1) it was passed without the due hearing required by Section 10 of Republic Act No. 720, as amended; (2) defendants, in adopting said resolution, have exceeded their authority of supervision granted them under the aforementioned section and (3) because in serving upon Lucena the original of the letter dated June 16, 1961, defendants were unnecessarily assisted by personnel from the Philippine Constabulary and the National Bureau of Investigation, a fact which has caused scandal and prejudice to Lucena and led to the newspaper publications mentioned heretofore and which has instilled an unfounded fear in its depositors and clients, destroying their confidence in her.

Defendants' answer to the complaint, on the other hand, alleged that they are empowered, under Republic Acts 265, 337 and 720, as amended, to promulgate the resolution in question; that the Director of the Department of Rural Banks of the Central Bank is duly vested by law with the duty of supervising the establishment, operation and management of rural banks created in accordance with the Rural Banks Act, as amended, and, finally, that

the present action was premature as defendants have not exhausted all administrative remedies. Their amended answer further alleged "that Rural Bank is in such condition of insolvency, or that its continuance in business would involve probable loss to depositors and creditors, as would require the Monetary Board to adopt the measures in said Resolution No. 928 even without hearing since under Section 29 of Republic Act 265 defendants-appellants are authorized to forbid the Rural Bank to do business, to take charge of its assets (not to take over management) and to cause its reorganization and place it in a condition to enable it to continue in business with safety to creditors and depositors" (pp. 35-36, Amended Answer, pp. 421-458, Vol. I, rec.).

After due trial, the lower court rendered the appealed judgment, from which, as stated heretofore, both parties appealed.

In spite of the numerous errors which Lucena and the Central Bank claim were committed by the trial court, there is really but one issue decisive of their appeals, namely: the validity of Resolution No. 928 of the Monetary Board which, in the opinion of the trial judge, amounted to a directive to take over the management of Lucena, without the latter having been given due hearing.

Rural banking in the Philippines is governed by Section 10 of Republic Act 720, as amended, which reads as follows:

"SEC. 10. The power to supervise the operation of any Rural Bank by the Monetary Board of the Central Bank as herein indicated, shall consist in placing limits to the maximum credit allowed any individual borrowers; in prescribing the interest rate; in determining the loan period and loan procedures; in indicating the manner in which technical assistance shall be extended to Rural Banks; in imposing a uniform accounting system and manner of keeping the accounts and records of the Rural Banks; in undertaking regular credit examination of the Rural Banks; in instituting periodic surveys of loans and lending procedures, audits, test check of cash and other transactions of the Rural Banks, in conducting training courses for personnel of Rural Banks; and, in general, in supervising the business operation of the Rural Banks.

The director of the Department of Central Bank designated by the Monetary Board to supervise the Rural Banks shall have the power to enforce the law, orders, instructions, rules and regulations promulgated by the Monetary Board applicable to Rural Banks; to require Rural Banks, their directors, officers and agents to conduct and manage the affairs of the Rural Bank in a lawful and orderly manner; and, upon proof that the Rural Bank or its Board of Directors or officers are conducting and managing the affairs of the bank in a manner contrary to law, orders, instructions, rules and regulations promulgated by the Monetary Board or in a manner substantially prejudicial to the interests of the government, depositors, or creditors, to take over the management of such bank when specifically authorized to do so by the Monetary Board after due hearing until a new board of directors and officers are elected and qualified without prejudice to the prosecution of the persons responsible for such violations under the provisions of section thirty-two, thirty-three, and thirty-four of Republic Act Numbered two hundred sixty-five.

The management of the Rural Bank by the Central Bank shall be without expense to the Rural Bank, except such is actually necessary for its operation, pending the election and qualification of a new board of directors and officers to take the place of those responsible for the violations or acts contrary to the interests of the government, depositors or creditors.

The director and the examiners of the Department of the Central Bank charged with the supervision of Rural Banks are hereby authorized to administer oaths to any director, officer or employee of any Rural Bank or to any voluntary witness and to compel the presentation of all books, documents, papers or records necessary in his or their judgment to ascertain the facts relative to the true condition of any Rural Bank or to any loan. (As Amended by Republic Act No. 2670, Section 2.)"

Besides granting supervisory power to the Monetary Board over rural banks and enumerating the different

matters over which such supervisory power may be exercised, the above-quoted legal provision like-wise grants the Monetary Board authority (a) to designate a Director for the Department of the Central Bank that will supervise rural banks. This officer actually known as Director of the Department of Rural Banks has, in turn, authority: (1) to enforce the law, orders, instructions, rules and regulations promulgated by the Monetary Board applicable to rural banks; (2) to require rural banks, the Directors, officers and agents to conduct and manage the affairs of the rural bank in a lawful and orderly manner, and upon proof that any particular rural bank or its board of directors or officers is or are conducting and managing the affairs of said bank in a manner contrary to law, orders, instructions, rules and regulations promulgated by the Monetary Board, or in a manner substantially prejudicial to the interest of the government, depositors or creditors, "to take over the management of such bank when specifically authorized to do so by the Monetary Board after due hearing etc". This provision defining the authority and providing for the duties of the Director of the Department of Rural Banks finds partial implementation in the provisions of Section 79 of the Rules and Regulations governing rural banks (Exh. 19-Stipulation), which provides, inter alia, that said Director may forbid any rural bank from carrying on any transaction which it deems unlawful or prejudicial to the interest of the government, or of the depositors or creditors of the bank, or contrary to the policies and objectives of the Rural Banks Act.

Section 27 of Republic Act 720, on the other hand, makes as part thereof the provisions of Republic Acts 265 (the Central Bank Act) and 337 (which regulates banks and banking institutions in the Philippines and provides for other purposes) in so far as they are applicable and not in conflict with any of its own provisions.

Resolution No. 928 of the Monetary Board is of the following tenor:

"928. Report of the Department of Rural' Banks on the examination of the Rural Bank of Lucena, Inc.; report of the Director, Department of Rural Banks, on the hearing regarding the said report scheduled by the Monetary Board and held at the Department of Rural Banks on June 10, 1961.

"The Acting Governor presented the following to the Board:

"1. A preliminary report of the Director, Department of Rural Banks, dated June 6, 1961, on the examination of the Rural Bank of Lucena, Inc. as of March 18, 1961; and

"2. A report of the Director, Department of Rural Banks, dated June 12, 1961 on the hearing scheduled by the Monetary Board to be held at the Department of Rural Banks on June 10, 1961 with regard to the said preliminary report.

(After the Board heard the report of the Director, Department of Rural Banks, on what transpired during the aforesaid scheduled hearing on June 10, 1961, and after the Board had agreed on the steps to be taken in connection with the findings of the Central Bank examiners on the operation of the Rural Bank of Lucena, Inc., Judge Sixto de la Costa and Atty. Roberto Diokno were ushered into the Conference Room).

"At the outset, the Acting Governor informed the representatives of the Rural Bank of Lucena, Inc. of the decision of the Monetary Board (a) to request the Board of Directors of the Rural Bank of Lucena, Inc. to convene immediately a stockholders' meeting for the purpose of electing a new Board of Directors acceptable to the Central Bank; (b) to withdraw or limit certain functions of the Rural Bank, such as acceptance of deposits from new depositors, granting of new loans, issuance of drafts, and making of disbursements; and (c) to assign Central Bank examiners to oversee the operations of the Rural Bank. He pointed out, however, that the Central Bank has not yet taken over the management of the Rural Bank.

"Judge de la Costa stated that the Rural Bank of Lucena, Inc. had not been given a fair hearing; that it had not been afforded a chance to disprove the charges, if any, against the bank because it had not been informed of the nature of the charges.

"The Director, Department of Rural Banks, said, however, that the Rural Bank of Lucena, Inc. had been given due and fair hearing as required by law, as he had explained in his aforesaid report dated June 12, 1961.

"The Officer-in-Charge, Office of the Legal Counsel, informed the Board that the procedure as planned was to show to the representatives of the Lucena Rural Bank, Inc. the report of the Director of the Department of Rural Banks and copies of the evidence, excluding that portion of the report which contains the analysis of the Rural Bank's financial statement and the recommendations intended only for the Monetary Board, and then the representation of the Lucena Rural Bank, Inc. were in turn to present their evidence. These would have been the preliminary steps before some remedial measures could be arrived at.

"According to the aforementioned Officer-in-Charge, Atty. Jose W. Diokno arrived at about 11:00 a.m. so that nothing substantial could have been accomplished at the conference. He appeared to be unwilling to talk about his evidence over the conference table as shown by the fact that he had not brought any papers with him. Confronted with the report and the evidence, he asked for a copy of the complete report of the Department of Rural Banks but the Director thereof refused to furnish him the full report, as the aforementioned portion thereof are not necessary in the evaluation of the examiners' findings. At this juncture, Atty. Diokno made the statement that he did not consider the conference as a due hearing. So the Director of the said Department stopped the conference.

"The Officer-in-Charge also stated that Atty. Diokno had been properly apprised of the charges or findings regarding fictitious loans, padded loans, low and non-existent collaterals and deficient reserve; that Atty. Diokno had been furnished with the pertinent schedules, that in an administrative proceeding, it is enough that the complaint recites the substance of the charges; and that in the presentation of evidence, too much technicalities should be avoided. The Director of the Department of Rural Banks considered the above-mentioned financial analysis and recommendations as highly confidential and intended only for the Monetary Board and that their disclosure to the management of the Lucena Rural Bank Inc. at the moment would be premature.

"President Romualdez likewise, stated that there was no dispute with respect to the reserve deficiencies of the Rural Bank. In this connection he said, the Central Bank examiners did not make any charge; they merely reported a finding as gathered from the books of the Rural Bank itself. Thus, there was no alternative on the part of the Central Bank but to stop the Rural Bank from granting new loans to protect the interest of its depositors.

"Judge de la Costa stated that the Rural Bank of Lucena, Inc. had been examined consecutively during the last three years, and every time an examination thereof was conducted a run on the bank always followed thereby resulting in deficiencies in its reserves.

"With the aid of a graph showing the relationship of the receipt of deposits and the net cash position of the bank to the loans granted by the bank, the Director, Department of Rural Banks, disproved Judge de la Costa's foregoing allegation. According to the said Director, while the deposits of the bank remained more or less steady, loan investments went so high that its net cash assets took a nose dive.

(Judge de la Costa and Atty. Roberto Diokno left the Conference Room after making their representations to the Board.)

"The Monetary Board, after due hearing, in which the Lucena Rural Bank, Inc. was given ample opportunity to be heard, has found, as sufficiently established by the evidence presented, that the officers, directors and employees of the Lucena Rural Bank, Inc. committed the following acts: (1) granting fictitious loans out of the funds of the rural bank; (2) granting loans inflated in the books of the rural bank; (3) granting loans secured by real estate properties which are either non-existent or whose values have been over-inflated; (4) granting loans to individuals and corporations that are not eligible and not qualified as borrowers of a rural bank under Sec. 5 of Republic Act No. 720, as amended; (5) permitting the Rural Bank to be chronically

deficient in its avail-able reserve against deposit liabilities; (6) authorizing the sale of domestic drafts without sufficient covering funds with the depository bank; and (7) failure to record in the books of the Rural Bank substantial expenditures incurred by the bank.

"The foregoing acts committed by the officers, directors and employees of the Rural Bank of Lucena, Inc. being substan-tially prejudicial to the interest of the Government, depositors or creditors, it appearing that the continuance in business of the said Rural Bank under such circumstances would involve probable loss to its creditors or depositors; and it having been shown further that notwithstanding warnings and directives of the Director, Department of Rural Banks, the aforesaid officers, di-rectors and employees of the Lucena Rural Bank, Inc. persisted in such unsafe and unsound banking practices which are in violation of the laws, instructions, orders, rules and regulations promulgated by the Mo-netary Board, the Board pursuant to Section 106 of Republic Act 720, as amended, and Section 10 of Republic Act 265, after due deliberation and by unanimous vote, decided as follows:

"1. To direct the Board of Directors of the Rural Bank of Lucena, Inc. to convene within five (5) days upon receipt of this decision, a stockholders' meeting for the pur-pose of reorganizing the said bank and electing a new board of directors acceptable to the Central Bank;

"2. To authorize the management to send Central Bank representatives to the said stockholders' meeting so as to fully inform the stockholders of (a) the findings of the Monetary Board on the operations of the Rural Bank; and (b) the instructions of the Board regarding the reorganization of the bank for the protection of the interests of the Government and the depositors and stockholders of the bank;

"3. To direct the Rural Bank of Lucena, Inc., upon receipt of this decision of the Monetary Board:

- a. Not to grant new loans or renewals;
- b. Not to accept deposits from new depositors;
- c. To service only the deposit accounts of existing depositors;
- d. Not to issue drafts without the prior approval of the Central Bank examiners to be assigned to over-see the operation of the rural bank; and
- e. Not to make any disbursements with-out the prior approval of the said Central Bank examiners;

"4. To inform the Rural Bank of Lucena, Inc. that in the event of non-compliance with paragraphs 1 and 3 above by the Rural Bank of Lucena, Inc., or if the said Rural Bank takes any step that would prevent the im-plementation of the directives contained in paragraphs 1 and 3 above, the Central Bank shall exercise its duty under the law to take over the management of the said Rural Bank; and

"5. To authorize the management (a) to ask the assistance of the Philippine Constabulary, the National Bureau of Investigation and other government agencies, if the circumstances so warrant, in the investigation of the Lucena Rural Bank, Inc.

"The Board simultaneously confirmed the foregoing decisions."

x x x x x x x x

(Par. 30, Partial Stipulation of Facts, pp. 18-19, folder 1 of exh.)

As stated heretofore, the appeals before Us depend entirely upon the question of whether or not the above re-solution is valid - because it was issued in the exercise of the supervisory jurisdiction of the Central Bank – or it is void -because it amounts to "taking over the management" of Lucena, without giving it a previous opportunity to be heard.

The supervisory jurisdiction of the Central Bank over Lucena and all rural banks is admitted. Neither may it be successfully denied that, to exercise said jurisdiction, the Central Bank need not give a previous hearing to the rural bank that will be affected by whatever action it may decide to take in connection with the latter's business or operation. Indeed, to require such a previous hearing is not only impractical but would tend to defeat the very purpose of the law when it invested the Central Bank with such authority.

Upon the other hand, it is clear from the very wording of the law and implementing Central Bank regulations that before the Central Bank may "take over" the management of any rural bank the latter must be heard.

It only remains now to determine whether the directives contained in the questioned resolution amount to the Central Bank "taking over" the management of Lucena, or are measures "supervisory" in character.

The first directive enjoins the Board of Directors of Lucena to convene, within five (5) days from receipt of the questioned resolution, a stockholders meeting for the purpose of re-organizing the Bank and electing members of a new Board of Directors acceptable to the Central Bank. By this directive the Central Bank did not call nor hold a stockholders' meeting; much less did it elect the members of the Board of Directors of Lucena. It simply enjoined the latter to hold a stock-holders' meeting, and proceed to elect the members of a new Board, subject only to the condition that they should be acceptable to the Central Bank.

In this connection We can not lose sight of the fact that the Government has a considerable monetary investment in Lucena. Its interest in the proper management of the latter's affairs is therefore dictated by self interest as well as by public policy. In fact, the law imposes upon the Monetary Board the duty to protect that investment of the Government by seeing to it that Lucena is at all times managed by men of character and integrity. The provisions of Section 1, Article IV of the By-Laws of Lucena (Exh. 12-Stipulation, p. 54, Folder of Exhibits) themselves are to the effect that the qualifications of the members of the Board of Directors shall be subject to the approval of the Central Bank. Upon the other hand, under Section 9 of Republic Act 337, the Monetary Board may withhold or refuse to issue the certificate of authority mentioned therein - which is a pre-requisite for the registration of the Articles of Incorporation, or any amendment thereof, of any bank - unless said Monetary Board is satisfied, upon the evidence submitted to it, with the integrity and responsibility of its organizers and administrators. There being no reason why this provision should not apply to rural banks as well, the conclusion becomes inescapable that the Monetary Board may also withhold the issuance of said certificate of authority upon the ground aforesaid. If it may legally do this, why may it not have authority to require a re-organization of the Board of Directors of any bank or rural bank if, as in the present case, it had found after proper investigation, that the incumbent members had mis-managed the affairs of the bank?

Under the second directive, representatives of the Central Bank are authorized to be present at the stockholders' meeting but only for the purpose of (a) informing them of the findings of the Monetary Board in connection with the operations of Lucena, and (b) of the instructions of said Board relative to the re-organization of Lucena. As is obvious this was dictated by the necessity of acquainting the stockholders with the reasons that prompted the Central Bank to order the re-organization of Lucena, with the end in view that such information may serve them as guide in the election of the new members of the Board of Directors. Singly or jointly with the other directives, this one gives Us no reason to say that the Central Bank had "taken over" the management of Lucena. Considering the acts of mismanagement and irregularities discovered by the examiners of the Central Bank in the conduct of the business operations of Lucena, it was imperative that the same be brought to the attention of the latter's stockholders before they proceeded to elect those who would compose the membership of the new Board.

The third directive enjoins Lucena not to grant new loans or renewals nor to accept new depositors; to service only the deposit accounts of existing depositors; not to issue drafts without prior approval of the Central Bank

examiners who would oversee its operations; and finally, not to make new disbursements without prior approval of said examiners.

In the circumstances of the case, it was to be assumed that all these limitations upon the scope of the operations of Lucena were intended to be temporary in nature. They were security measures urgently demanded by the irregularities discovered by the Central Bank examiners mentioned at the beginning of this opinion. They were intended to protect not only the funds already deposited with Lucena but also prospective depositors who might have had no knowledge or information regarding the manner in which the funds of Lucena had been administered previously. As these measures - We repeat - were intended to be enforced only during the period of re-organization and until the Central Bank was satisfied that the new members of the Board of Directors of Lucena were conducting its affairs in accordance with law and in the interest of all concerned, We are satisfied that they fall well within the broad supervisory powers of the Central Bank over Lucena and other rural banks.

The fourth directive is a warning that should Lucena fail or refuse to comply with the first and third directives, or if it took any step calculated to prevent their implementation, the Central Bank would then exercise its right under the law to "take over" its management. Rather than constitute evidence of "taking over", this particular directive goes a long way to show just the opposite.

Finally, the fifth directive authorizes the management to secure the assistance of the Philippine Constabulary, the National Bureau of Investigation and other governmental agencies, should circumstances so warrant, in the investigation of the affairs of Lucena. This is sanctioned by Section 20 of Republic Act 720, as amended. As it clearly provides for something that would be resorted to only in case of absolute necessity, and there being no showing that the Central Bank had actually asked for the assistance of the agencies' mentioned heretofore and that the latter, by directive of the Central Bank, had interfered directly with the management and operations of Lucena, there is no ground to hold that by this last directive the Central Bank had "taken over" the management of said Bank.

We summarize our views as follows: from the very provisions of the questioned resolution, it appears that the intention of the Central Bank was to provide for temporary measures to prevent the commission of further irregularities in the business operations of Lucena; to provide for the placing of its management in the hands of men of integrity and competence; to provide for authority for its examiners to oversee the operations of Lucena, and finally, to serve a warning upon the latter that should it refuse to comply with the directives contained in the questioned resolution, the Central Bank would then have no other recourse but to do its duty under the law - to "take over" the management and operations of Lucena - for the protection of the interest of the Government and of the stockholders.

Consequently, We are of the opinion and so hold, that the questioned resolution falls within the scope of the supervisory authority that the Central Bank has over Lucena and other banks of a similar nature.

Having arrived at the above conclusion, We deem it unnecessary to discuss the other questions raised by both parties in their respective briefs.

WHEREFORE, the appealed decision is reversed and set aside, and the basic petition filed in this case is dismissed, with costs.

Concepcion, C.J., Reyes, J.B.L., Makalintal, Zaldivar, Sanchez, Castro, Teehankee, and Barredo, JJ., concur.
Fernando, J., did not take part.

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