SECURITIES AND EXCHANGE COMMISSION, PETITIONER, VS. PERFORMANCE FOREIGN EXCHANGE CORPORATION, RESPONDENT.

G.R. NO. 154131. July 20, 2006

Ponente: SANDOVAL-GUTIERREZ, J.

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SANDOVAL-GUTIERREZ, J.:

For our resolution is the Petition for Review on Certiorari[1] assailing the Decision[2] dated February 11, 2002 and Resolution dated July 3, 2002 of the Court of Appeals in CA-G.R. SP No. 65217, entitled "Performance Foreign Exchange Corporation, petitioner, versus Securities and Exchange Commission, respondent."
The pertinent facts as found by the Court of Appeals are:

Performance Foreign Exchange Corporation, herein respondent, is a domestic corporation duly registered on June 23, 1998 under Securities and Exchange Commission (SEC) Registration No. A199808910, with the following purposes:

> Primary Purpose
>
> To operate as a broker/agent between market participants in transactions involving, but not limited to, foreign exchange, deposits, interest rate instruments, fixed income securities, bonds/bills, repurchased agreements of fixed income securities, certificate of deposits, bankers acceptances, bills of exchange, over-the-counter option of the aforementioned instruments, Lesser Developed Country's (L.D.C.) debt, energy and stock indexes and all related, similar or derivative products, other than acting as a broker for the trading of securities pursuant to the Revised Securities Act of the Philippines.
>
> Secondary Purpose
>
> To engage in money changer or exchanging foreign currencies into domestic currency, Philippine currency or other foreign currencies into another currencies.

After two years of operation, respondent received a letter dated November 28, 2000 from the SEC, herein petitioner, requiring it to appear before the Compliance and Enforcement Department (CED) on December 14, 2000 for a clarificatory conference regarding its business operations. Respondent's officers complied and explained before the CED the nature of their business.

On January 16, 2001, Emilio B. Aquino, Director of CED, issued a Cease and Desist Order,[3] in CED Case No. 99-2297, stating that his department conducted an inquiry on respondent's business operations for possible violation of Republic Act (R.A.) No. 8799 (otherwise known as The Securities Regulation Code); that the outcome of the inquiry shows that respondent is engaged in the trading of foreign currency futures contracts in behalf of its clients without the necessary license; that such transaction can be deemed as a direct violation of Section 11 of R.A. No. 8799[4] and the related provisions of its Implementing Rules and Regulations; and that it is imperative to enjoin respondent from further operating as such to protect the interest of the public. The dispositive portion of the said Order reads:

> WHEREFORE, pursuant to the authority vested in the Commission, PERFORMANCE FOREIGN EXCHANGE CORPORATION, its officers, directors, agents, representatives, and any and all persons claiming and acting under their authority, are hereby ordered to immediately CEASE AND DESIST from further engaging in the solicitation of funds for foreign currency trading and operating as a foreign currency futures merchant/broker, upon receipt of this Order.
>
> In accordance with the provisions of Section 64.3[5] of Republic Act 8799, otherwise known as the Securities Regulation Code, the parties subject of this Cease and Desist Order may file a request for the lifting thereof within five (5) days from receipt hereof.
>
> SO ORDERED.

On January 25, 2001, respondent filed with petitioner SEC a motion[6] praying for the lifting of the Cease and Desist Order, alleging that: (a) it has not violated any law or regulation in the conduct of its business; (b) it has been operating in accordance with the purposes for which it was organized, which purposes were duly approved by petitioner; (c) it has not engaged in currency futures contracts trading; and (d) its business involves "spot currency trading which is not a form of currency futures transaction."

On February 8, 2001, then SEC Chairman Lilia R. Bautista, in her desire to know with certainty the nature of respondent's business, sent a letter[7] to the Bangko Sentral ng Pilipinas (BSP), requesting a definitive statement that respondent's business transactions are a form of financial derivatives and, therefore, can only be undertaken by banks or non-bank financial intermediaries performing quasi-banking functions.

Without waiting for BSP's determination of the matter, petitioner, the following day (February 9, 2001), issued an Order[8] denying respondent's motion for the lifting of the Cease and Desist Order and directing that the same stays until respondent shall have submitted the appropriate "endorsement" from the BSP that it can engage in financial derivative transactions. The Order states that the contracts entered into, offered and sold by respondent are in the nature of commodity futures contracts;[9] and that such contracts may be considered a form of financial derivatives instruments, the trading of which is regulated by BSP.

On February 16, 2001, respondent filed a Manifestation With Urgent Motion[10] praying that, pending determination by the BSP of the real nature of its business, the implementation of the February 9, 2001 Order be temporarily suspended to allow it to continue its operations.

On March 15, 2001, respondent, in compliance with petitioner's February 9, 2001 Order requiring it to submit the appropriate BSP "endorsement," presented before the BSP panel of officers a summary of its operations and its foreign exchange spot product.

On April 23, 2001, petitioner issued an Order[11] making the Cease and Desist Order permanent, thus:

> WHEREAS, on February 19, 2001, PFEC filed with the Commission its "Manifestation with Urgent Motion to Temporarily Suspend Implementation of Order dated 09 February 2001," which Manifestation was denied by the Commission en banc during its meeting on February 22, 2001, and the said denial was conveyed verbally to the corporation;
>
> WHEREFORE, premises considered, and pursuant to the authority vested in the Commission, the Cease and Desist Order is now made permanent, and Performance Foreign Exchange Corporation is hereby directed to show cause within thirty (30) days from receipt of this Order why its certificate of registration should not be revoked for violation of the Securities Regulation Code, and/or PD 902-A specifically on the ground of serious misrepresentation as to what the corporation can do or is doing, to the great prejudice or damage to the general public. (Underscoring supplied)

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On May 4, 2001, respondent filed a motion[12] praying that the said Order be set aside. Petitioner, however, did not act on the motion. This prompted respondent to file with petitioner a notice[13] dated June 14, 2001 that it is withdrawing its motion in order to seek a more appropriate and speedy remedy.

Feeling the injurious effects of petitioner's acts to its business operations, respondent, on June 20, 2001, filed with the Court of Appeals a Petition for Certiorari[14] with prayer for a temporary restraining order and preliminary injunction, docketed as CA-G.R. SP No. 65217. Respondent alleged, among others, that petitioner SEC acted without or in excess of its jurisdiction or with grave abuse of discretion when it issued the Cease and Desist Order and its subsequent Order making the same permanent without waiting for the BSP's determination of the real nature of its business operations; and that petitioner's Orders, issued without any factual basis, violated its (respondent's) fundamental right to due process.

Meanwhile, on August 13, 2001, Amado M. Tetangco, Jr., then Officer-in-Charge, Office of the Governor, BSP, in answer to SEC Chairman Lilia Bautista's letter-request of February 8, 2001, stated that respondent's business activity "does not fall under the category of futures trading" and "can not be classified as financial derivatives transactions," thus:

> Dear Ms. Bautista,
>
> This refers to your letter dated February 8, 2001 requesting for a definitive statement that the foreign currency leverage trading engage in by private corporations, particularly, Performance Foreign Exchange Corporation (PFEC), is a financial derivatives transaction and that it can only be undertaken by banks or non-bank financial intermediaries performing quasi-banking functions and/or its subsidiaries/affiliates.
>
> As indicated in your description of the transactions and the documents submitted, the foreign currency leverage trading, subject of your query, is essentially similar in mechanics to currency future trading, particularly with respect to the margin requirements, standard contract size, and daily market-to-market of open position. However, it does not fall under the category of futures trading because it is not exchange-traded. Further, we can not classify it as being financial derivatives transactions as we consider the transaction as plain currency margin trading, which by its mechanics, involve the set-up of margin and non-delivery of the currencies involved.
>
> In view of the foregoing facts, the activities of the aforesaid corporation are not covered by BSP guidelines on derivative licensing.
>
> We hope we have satisfactorily clarified your concerns.
>
> Very truly yours,
>
> (Sgd.)
> AMANDO M. TETANGCO, JR.[15]

On February 11, 2002, the Court of Appeals rendered a Decision[16] in favor of respondent, thus:

> WHEREFORE, premises considered, the instant petition is GRANTED and accordingly, the assailed Orders dated January 16, 2001, February 9, 2001, February 22, 2001 and April 23, 2001 of the Securities and Exchange Commission are SET ASIDE.
> SO ORDERED.

The Court of Appeals ruled that petitioner acted with grave abuse of discretion when it issued its challenged Orders without a positive factual finding that respondent violated the Securities Regulation Code.

Petitioner filed a motion for reconsideration but it was denied by the appellate court in a Resolution[17] dated July

3, 2002.

Hence, the instant Petition for Review on Certiorari.

Petitioner, through the Solicitor General, contends that the Court of Appeals erred in not applying the rule that factual findings of quasi-judicial bodies, like the SEC, which have acquired expertise because their jurisdiction is confined to specific matters, are generally accorded not only respect but even finality if such findings are supported by substantial evidence.[18]

In its Comment,[19] respondent counters that the instant petition utterly lacks merit and should be dismissed.

The issue for our resolution is whether petitioner SEC acted with grave abuse of discretion in issuing the Cease and Desist Order and its subsequent Order making it permanent.

Section 64 of R.A. No. 8799, provides:

> Sec. 64. Cease and Desist Order. - 64.1. The Commission, after proper investigation or verification, motu proprio, or upon verified complaint by any aggrieved party, may issue a cease and desist order without the necessity of a prior hearing if in its judgment the act or practice, unless restrained, will operate as a fraud on investors or is otherwise likely to cause grave or irreparable injury or prejudice to the investing public.
>
> x x x. (Underscoring supplied)

Under the above provision, there are two essential requirements that must be complied with by the SEC before it may issue a cease and desist order: First, it must conduct proper investigation or verification; and Second, there must be a finding that the act or practice, unless restrained, will operate as a fraud on investors or is otherwise likely to cause grave or irreparable injury or prejudice to the investing public.

Here, the first requirement is not present. Petitioner did not conduct proper investigation or verification before it issued the challenged orders. The clarificatory conference undertaken by petitioner regarding respondent's business operations cannot be considered a proper investigation or verification process to justify the issuance of the Cease and Desist Order. It was merely an initial stage of such process, considering that after it issued the said order following the clarificatory conference, petitioner still sought verification from the BSP on the nature of respondent's business activity. Its letter to the BSP dated February 8, 2001 states in part:

> The Securities and Exchange Commission has been investigating corporations which engage in foreign currency trading abroad. The following illustrates their operations:
>
> x x x
>
> Enclosed are pertinent documents which were submitted by a corporation showing how its transactions operate. It is claimed by the corporation in question that theirs are all spot transactions and are not covered by the Bangko Sentral ng Pilipinas. We understand, however, that in other jurisdiction, this type of activity can only be done by banks.
>
> Previous inquiries from the Bangko Sentral ng Pilipinas, specifically Department of Commercial Banks II, and your department, Commercial Banks I, lead to conclude that this kind of trading in foreign currencies may be a form of financial derivatives.
>
> May we, therefore, request a definitive statement that the above-described transactions, and as illustrated in the attached documents, are a form of financial derivatives and, therefore, can only be undertaken by banks, or non-bank financial intermediaries performing quasi-banking functions and/or its subsidiaries/affiliates.[20] (Underscoring supplied)

Petitioner's act of referring the matter to the BSP is an essential part of the investigation and verification process. In fact, such referral indicates that petitioner concedes to the BSP's expertise in determining the nature of respondent's business. It bears stressing, however, that such investigation and verification, to be proper, must be conducted by petitioner before, not after, issuing the Cease and Desist Order in question. This, petitioner utterly failed to do. The issuance of such order even before it could finish its investigation and verification on respondent's business activity obviously contravenes Section 64 of R.A. No. 8799 earlier quoted.

Worse, when respondent filed a motion praying that the same order be lifted for being premature, petitioner, in its Order dated February 9, 2001, even denied the motion despite its admission therein that it cannot determine certain material facts involving respondent's transactions and, as such, the matter must be referred to the BSP for determination, thus:

> In the light of the above circumstances, and the fact that the Commission cannot determine whether such transactions are actually executed in Singapore or Hongkong as alleged, and whether the foreign currency rates used in the transactions are verifiable, it is our position that the same be endorsed to the BSP.
>
> In view of the foregoing, the cease and desist order stays against the corporation until the latter shall be able to submit the appropriate endorsement from the Bangko Sentral ng Pilipinas that it can engage in financial derivative transactions.
>
> SO ORDERED.[21] (Underscoring supplied)

And worst, without waiting for BSP's action, petitioner proceeded to issue its Order dated April 23, 2001 making the Cease and Desist Order permanent. In the same Order, petitioner further directed respondent "to show cause x x x why its certificate of registration should not be revoked for alleged violation of the Securities Regulation Code and/or Presidential Decree No. 902-A, specifically on the ground of serious misrepresentation as to what the corporation can do or is doing to the great prejudice or damage to the general public." Obviously, without BSP's determination of the nature of respondent's business, there was no factual and legal basis to justify the issuance of such order.

Which brings us to the second requirement. Before a cease and desist order may be issued by the SEC, there must be a showing that the act or practice sought to be restrained will operate as a fraud on investors or is likely to cause grave, irreparable injury or prejudice to the investing public. Such requirement implies that the act to be restrained has been determined after conducting the proper investigation/verification. In this case, the nature of the act to be restrained can only be determined after the BSP shall have submitted its findings to petitioner. However, there is nothing in the questioned Orders that shows how the public is greatly prejudiced or damaged by respondent's business operation.

In sum, we find no reversible error committed by the Court of Appeals in rendering its assailed Decision and Resolution.

WHEREFORE, we DENY the petition. The challenged Decision and Resolution of the Court of Appeals in CA-G.R. SP No. 65217 are AFFIRMED.

SO ORDERED.

Puno, (Chairperson), Corona, Azcuna, and Garcia, JJ., concur.

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[1] Filed under Rule 45, 1997 Rules of Civil Procedure, as amended.

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[2] Penned by Associate Justice Remedios A. Salazar-Fernando and concurred in by Associate Justice Romeo J. Callejo, Sr. (now a member of this Court) and Associate Justice Perlita J. Tria-Tirona (retired).

[3] Annex "C," Petition, rollo, pp. 56-57.

[4] Sec. 11. Commodity Futures Contracts. - No person shall offer, sell or enter into commodity futures contracts except in accordance with the rules, regulations and orders the Commission (SEC) may prescribe in the public interest. The Commission shall promulgate rules and regulations involving commodity futures contracts to protect investors to ensure the development of a fair and transparent commodities market.

[5] Sec. 64.3. Any person against whom a cease and desist order was issued may, within five (5) days from receipt of the order, file a formal request for a lifting thereof. Said request shall be set for hearing by the Commission not later than fifteen (15) days from its filing and the resolution thereof shall be made not later than ten (10) days from the termination of the hearing. If the Commission fails to resolve the request within the time herein prescribed, the cease and desist order shall automatically be lifted.

[6] Annex "I," Petition, rollo, pp. 145-157.

[7]Annex "F," id., pp. 224-225.

[8] Annex "D," id., pp. 58-61.

[9] The Order cited the Implementing Rules and Regulations of the Securities Regulation Code defining commodity futures contract as "a contract providing for the making or taking delivery at a prescribed time in the future of a specific quantity and quality of a commodity or the cash value thereof, which is customarily offset prior to the delivery date, and includes standardized contracts having the indicia of commodity futures, commodity options and commodity leverage, or margin contracts." Id., p. 58.

[10] Annex "D," Respondent's Comment, id., pp. 432-436.

[11]Annex "E," Petition, id., pp. 62-63.

[12] Annex "H," id., pp. 226-230.

[13]Annex "I," id., p. 232.

[14] Filed under Rule 65 of the 1997 Rules of Civil Procedure, as amended.

[15] Respondent's Comment, rollo, pp. 374-375.

[16]Id., pp. 444-456.

[17] Id., p. 458.

[18] Petition, id., p. 23.

[19] Id., pp. 362-414.

[20] Id., pp. 224-225.

[21] Id., pp. 60-61.

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