

RADIO COMMUNICATIONS OF THE PHILIPPINES, INC. (RCPI), PETITIONER, VS. NATIONAL WAGES COUNCIL AND BUKLOD NG MANGGAGAWA SA RCPI-NFL, RESPONDENTS.

G.R. No. 93044. March 26, 1992

Ponente: GUTIERREZ, JR., J.

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GUTIERREZ, JR., J.:

The focal issue for the Court's determination is whether or not petitioner Radio Communications of the Philippines, Inc. (RCPI) was, as of December 31, 1985, a distressed employer entitled to exemption from compliance with Wage Order No. 6 for the year 1985-1986.

On October 26, 1984, the President of the Philippines promulgated Wage Order No. 6 which provided for the increase of statutory minimum wage rates and cost of living allowances in the private sector. Distressed enterprises, however, were granted exemption from compliance with said wage order for a period not exceeding two years.

On October 30, 1984, respondent National Wages Council (NWC) promulgated NWC Policy Guidelines No. 8 which spelled out the following criteria for exemption:

"SECTION 5. Criteria for Exemption.

A. Actual Losses

(1) In the case of stock corporation, partnership, single proprietorship or non-stock/non profit organization engaged in business activities or charging fees for their services:

(a) a full exemption of one (1) year may be granted when the accumulated losses as of the end of the period have impaired by 25% or more the paid up capital as of the end of the last full accounting period in the case of corporation, or losses for the period shall have impaired by 25% or more the total invested capital at the beginning of the last full accounting period in the case of partnership and single proprietorship" (Underscoring supplied) (Rollo, p. 7)

RCPI filed an application for exemption for the year 1984-1985 which was approved by the NWC. In approving the exemption, NWC stated:

"After a thorough study of the supporting documents on file and the supplemental pleadings relative to the above subject, the Executive Committee is of the opinion that RCPI'S continued operational losses in 1984 and 1985 and the undertaking under the Compromise Agreement dated October 24, 1985 under PD 1713 and Wage Order No. 1, in addition to the requirements of Wage Order Nos. 2, 3, 5 & 6, would directly contribute to the financial dislocation of the company, unless remedial measures are instituted to avert such situation." (Rollo, p. 24)

RCPI thereafter filed its second application for exemption for the year 1985-1986. This time, the NWC, on

December 29, 1986, disapproved the application on the ground that RCPI did not qualify as a distressed establishment because it had retained earnings of P10,278,275 in its unaudited balance sheet as of December 31, 1985.

RCPI filed four motions for reconsideration which were all denied by respondent NWC. In denying the fourth motion for reconsideration, the NWC justified its action by pointing out that RCPI was not a distressed company since it had retained earnings of P8,237,528 based on its audited balance sheet as of December 31, 1985.

Hence, this petition.

RCPI alleges that respondent NWC acted with grave abuse of discretion amounting to excess of jurisdiction in disapproving its second application for exemption.

To prove that its accumulated losses have impaired its capital by more than 25% thereby entitling it to continued exemption for the second year, petitioner RCPI advances the following computation:

Retained earnings as of December 31, 1984

Deduct: Net loss for 1985

Less: Appraisal Increment transferred to

Retained Earnings

P19,820,785

12,067,834

7,752,951

As of 1984

For 1985

P27,809,943

484,577

28,294,520

Accumulated losses absorbed by Appraisal

Increment

P20,541,569

Paid up capital

% of Impairment:

20,541,569

22,589,970

22,589,970

90%

(Petitioner's Memorandum, Rollo, p. 278. Figures used are based on audited financial statements.)

The petitioner proceeds with the assertion that while it had retained earnings of P8,237,528 as of 1985, such figure is in its entirety composed of appraisal increments which are purely theoretical increases resulting from the revaluation of its property and equipment and not actual or realized profits arising from business operations. (Rollo, p. 280) Hence, the petitioner contends that, while on paper RCPI may theoretically appear to be reaping revenues because of a positive retained earning balance, in reality it is suffering actual losses. (Rollo, p. 281) And since appraisal increments (not being earnings, profit or income) were erroneously transferred to constitute the entire retained earnings, then the same appraisal increments must be subtracted to get the actual accumulated loss of RCPI. (Rollo, p. 283) This accumulated loss, not the retained earnings figure appearing in the financial statement, is the basis for the computation of the minimum 25% capital impairment for purposes of exemption (Rollo, p. 280).

Based on the foregoing computation, RCPI's accumulated losses had impaired its paid-up capital by 90% and therefore it qualified as a distressed establishment entitled to such exemption. (Rollo, p. 283)

This is not the first time this issue has come before us. In our resolution in *Buklod ng Manggagawa sa RCPI-NFL v. Hon. Augusto Sanchez*, G.R. No. 77503, July 13, 1988, this Court sustained NWC's grant of exemption to RCPI under Wage Order No. 6 in spite of the fact that RCPI's retained earnings balance as of 1984 was also in positive terms. The Court affirmed the questioned NWC order which "found that private respondent (RCPI) was incurring losses in its operations, justifying its aforesaid exemption, a finding that appears to be based on a thorough study of the documents and pleadings on record."

Significantly, the Solicitor General after three extensions of time in the present case, from June 21, 1990 to August 24, 1990, stated that, after judicious scrutiny of the record and in consonance with applicable law and jurisprudence, he could not, without violating the law, sustain the findings of public respondent NWC. He asked to be excused from representing the NWC in this case.

To be exempt from Wage Order No. 6, the impairment formula applied by NWC is:

"Section 5. Criteria for Exemption:

A. Actual losses

1. In the case of stock corporation

x x x :

a) A full exemption of one (1) year may be granted when accumulated losses as of the end of the period have impaired by 25% or more the paid capital as of the end of the last full accounting period in case of corporation, x x x.

b) A partial exemption of six (6) months may be granted when accumulated losses as of the end of the period have impaired by 20% or more but less than 25% the paid up capital in the case of corporation x x x." (NWC Policy Guidelines No. 8, underscoring supplied) (Rollo, p. 55)

We note from the above that the impairment formula speaks of actual losses in contra-distinction to actual profit or income. The formula requires accumulated losses, not for that year alone but for a period of time backwards until the given cut off date.

Since the purpose of the wage exemption is to assist financially beleaguered companies, the distinction between real or actual income and theoretical earnings arising from accounting principles becomes important.

To arrive at a distinction, we first adopt certain definitions:

"Retained earnings (or income) - ? accumulated net income, less distributions to stockholders and transfers to paid-in capital accounts. x x x Also known by the older title earned surplus" (Eric L. Kohler, A Dictionary for Accountants, 5th Ed., p. 409)

"Earnings - - A general term embracing revenue profit, or income," (Id., p. 188)

"Income - - 1. Money or money equivalent earned or accrued x x x and arising from sales or rentals of any type of goods or services, commissions, interest, gifts, recoveries from damages and windfalls from any outside source.

2. Sales of goods or services; in this sense, the term is less used than formerly, revenue now being preferred.

3. An addition, a receipt; often in contrast with outgo; as, the income and outgo of stores.

4. x x x (b) the remainder of revenue after deducting costs of sales and operating other expenses (= net income)" (Id., pp. 249- 250).

"Profit - 1. A general term for the excess of revenue, proceeds, or selling price over related costs; any pecuniary benefit arising from a commercial operation, from the practice of a profession, or from one or more individual transactions of any person." (Id., p. 379).

"Revenue - 1. Sales of products, merchandise and services, and earnings from interest, dividends, rents and wages; transactions resulting in increases in assets." (Id., p. 410).

FURTHER:

"Retained Earnings (or Earned Surplus) is the accumulated amount of profits and earnings of the business which has not been capitalized, offset by losses, or given out to stockholders as property dividends." (D.S. Pasion, Introductory Accounting, p. 195).

"The retained earnings is credited with the income of the period which may include:

- a. earnings of the business in its line of endeavor, such as the selling of merchandise or services;
- b. compensation received for the lending of capital, and
- c. profits or incomes of any kind resulting from the exchanges of assets.

It is debited with the loss of the period which may include:

- a. costs, expenses, and losses connected with its regular line of business.
- b. expenses and losses suffered in the financing of the business from outside sources, other than from stockholders,
- c. expenses and losses of any kind in the exchange of assets, and
- d. distribution of income earned to stockholders."

"Profit is the excess of the incoming assets over outgoing capital x x x." (Id., p. 291). (Rollo, pp. 58-59)

To add to the above, the Statement of Financial Accounting Standards No. 12 issued by the Accounting Standards Council defines certain terms as follows:

"Appraised or appraisal value, also termed as replacement cost or reproduction cost, is the revalued amount of property, plant and equipment determined by recognized specialists.

"Accumulated depreciation on appraisal, also termed as observed depreciation, is the accumulated depreciation

based on the appraised or appraisal value per appraiser's report.

"Sound value, also net appraised value, is the value per appraisal computed by deducting observed depreciation from appraised value.

"Net book value is computed by deducting accumulated depreciation on cost from historical cost.

"Appraisal increase is computed by deducting historical cost from appraised values.

"Revaluation increment is the excess of sound value over net book value." (At p. 4)

The transfer from revaluation increment on property to retained earnings representing the accumulated depreciation on appraisal increase already charged to operations was approved by the RCPI Board of Directors on April 12, 1982. The depreciation on appraisal increase previously deducted from actual income was added to retained earnings.

This transfer resulted in the P8,237,528.00 retained earnings pinpointed by the respondent NWC. Actually, this covers a six year period as follows:

"Retained Earnings as of 1979

Add: Net Income (Loss)

1980

1981

1982

1983

1984

1985

Dividends Declared

1980

1982

(P7,434,493)

(3,149,329)

2,630,447

1,579,916

(2,559,372)

(12,067,834)

T O T A L

P 799,642

2, 053,907

P3,797,215.00

(21,000,658.00)

(17,203,443.00)

(2,853,549.00)

Balance of Retained Earnings/Deficit as of 1985 - (P20,056,992.00)

Add: Transfer of portion of revaluation increment in

property to retained earnings

(depreciation on appraisal increase)

1980

1981

1982

1983

1984

1985

RETAINED EARNINGS AS OF 1985 (Rollo, pp. 141-142)

P8,571,430

7,526,837

4,316,459

3,927,412

3,467,805

484,577

28,294,520.00

P 8,237,528.00

RCPI argues that the amount of P28,294,520.00 representing the portion of revaluation increment (depreciation on appraisal increase) transferred to retained earnings should be deducted from the balance of retained earnings to arrive at the operational loss of P20,056,992.00.

The public respondent states that this is wrong because it would be tantamount to double deduction since said amount has already been yearly deducted from operations through additional depreciation charges starting 1980.

As earlier stated, the purpose of wage exemptions is to help financially distressed companies meet their labor costs without endangering the existence or viability of the firm upon which both management and labor depend for a living. Under the spirit of Wage Order No. 6, it is the actual ability of a firm to spend for its current needs and costs and not how the assets and liabilities of a firm may appear in the technical jargon of higher accounting

principles which is important. For instance, no matter how solid a firm may be in terms of essential fixed assets, its ability to pay daily payrolls will depend only on actual income unless some of the fixed assets are sold for wages and salaries.

True, the retained earnings account constitutes a company's accumulated profits or losses. However, it is not enough to treat said earnings as "earnings" in the real sense of the word for purposes of wage exemptions. We have to inquire into the true nature and composition of the retained earnings account.

The figures of the respondent NWC show that if we do not include the transfer of portions of revaluation increment in property to retained earnings, RCPI had an income deficit of P20,056,992 from 1980 to 1985. It is only when we add to the retained earnings account, the portion of the revaluation increment in property for the same period for a total of P28,294,520.00 that we get a positive retained earnings balance of P8,237,528.00. Without the transfer of the revaluation increment in property to the retained earnings account, there would be no positive balance. There would be a deficit.

Should we treat revaluation increment in property as income for purposes of determining wage levels?

To a company striving to meet daily payrolls, it is not of any comfort to say that the "appraisal increment transferred to retained earnings" represents actual earnings which were previously deducted from the actual net income figure through additional depreciation expense resulting from appraisal. In purely technical accounting terms, they may be considered as merely being returned not to the net income account but to the retained earnings balance to which the net income account is ultimately closed. This is to keep the books straight.

For purposes of compliance with the law on wage exemptions, however, the retained earnings arising from appraisal increment do not represent hard cash but merely theoretical increases resulting from upward valuations of old fixed assets. There is no income or profit from the sale of goods or services. No income is realized from the reappraisal of fixed assets until such a time as the machinery, equipment, and other fixed assets are sold or disposed of in the event of a liquidation of assets.

As stated in the preamble clauses of Wage Order No. 6, it is intended to enable workers to cope with price increases through the adjustment of their wages but "with due regard to insure increased productivity and viability of business and industry."

The NWC ruling treats the revaluation increment as similar to the sale of fixed assets. In the same way, however, that machinery and equipment should not be sold in order to meet increases in the wage of workers (for this would destroy not only the company but the employment of the workers themselves) so should a similar attitude be adopted when machinery or equipment is not sold but merely revalued.

On December 16, 1986, the NWC, through then Secretary Augusto B. Sanchez - its chairman, approved the application for exemption of RCPI and stated, among other things, that:

"The Executive Committee, therefore, recognizes the necessity to set aside technicalities required by existing criteria under NWC Policy Guidelines Nos. 6 and 8 and bestow greater significance to the actual financial condition of RCPI." (Rollo, p. 24; Emphasis supplied)

NWC decided to give RCPI a breathing spell because of numerous obligations that the company had to meet. Under a compromise agreement, RCPI bound itself to pay 30% of whatever was due the employees under PD 1713 for the mandatory third year increases and Wage Order No. 1 for the first and second year. The balance of 70% was subject to negotiations. (See G.R. No. 77503, *Buklod ng Manggagawa v. Sanchez*, supra, Rollo, p. 168). NWC found that RCPI's compliance with the Wage Orders would result in the company's financial dislocation and, accordingly, granted it the prayed for exemption.

We see no reason from the records why a different treatment should apply in the following year. Simply because there were changes or transfers of the same items to differently named accounts in the books of the company, it does not follow that it thereby ceased to be entitled to exemptions.

WHEREFORE, the petition is hereby GRANTED. The questioned decision and resolutions of the National Wages Council are SET ASIDE and the application for exemption from Wage Order No. 6 is GRANTED.

SO ORDERED.

Fernan, C.J., (Chairman), Bidin, Davide, Jr., and Romero, JJ., concur.
Feliciano, J., on leave.

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