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(In substitution of Senate Bill Nos. 1103, 1180 and 1762)

Prepared by the Committee on Banks, Financial Institutions and Currencies,
With Senators Drilon, Magsaysay and Madrigal, as authors.

AN ACT
GOVERNING THE ESTABLISHMENT, OPERATION AND REGULATION OF
LENDING COMPANIES

Be it enacted by the Senate and the House of Representatives of the Philippines in Congress assembled:

1 **Section 1.** *Title.* – This Act shall be known as the "Lending Company
2 Regulation Act of 2005".

3 **Section 2.** *Declaration of Policy.* – It is hereby declared the policy of the
4 State to regulate the establishment of Lending Companies and to place their
5 operation on a sound, efficient and stable condition to derive the optimum
6 advantages from them as an additional source of credit; to prevent and mitigate,
7 as far as practicable, practices prejudicial to public interest; and to lay down the
8 minimum requirements and standards under which they may be established and
9 do business.

10 **Section 3.** *Definition of Terms.* – For purposes of implementing this Act,
11 the following definitions shall apply:

12 a. *Lending Company* shall refer to a corporation engaged in granting
13 direct loans from their own funds or from other persons, not exceeding
14 nineteen (19) at any one time, with interest and charges whether on a
15 secured or unsecured basis, but shall not be deemed to include
16 banking institutions, investment houses, savings and loan associations,

1 financing companies, pawnshops, insurance companies, cooperatives
2 and other credit institutions already regulated by law. The term shall
3 be synonymous with *Lending Investors*.

4 b. *Debtor* shall refer to a borrower or person granted a loan by the
5 Lending Company.

6 c. *Quasi-Bank* shall refer to a non-bank financial institution authorized by
7 the BSP to engage in quasi-banking functions or in the borrowing of
8 funds from more than nineteen (19) lenders through the issuance,
9 endorsement or assignment with recourse or acceptance of deposit
10 substitutes as defined in Section 95 of Republic Act No. 7653 (the
11 "New Central Bank Act") for purposes of relending or purchasing of
12 receivables and other obligations.

13 d. *Subsidiary* shall refer to a corporation more than fifty percent (50%) of
14 the voting stock of which is owned by a bank or quasi-bank.

15 e. *Affiliate* shall refer to a corporation, the voting stock of which, to the
16 extent of fifty percent (50%) or less, is owned by a bank or quasi-
17 bank which is related or linked to such institution through common
18 stockholders or such other factors as may be determined by the
19 Monetary Board of the BSP.

20 f. *DTI* shall refer to the Department of Trade and Industry.

21 g. *BSP* shall refer to the Bangko Sentral ng Pilipinas.

22 **Section 4.** Bureau of Internal Revenue *Form of Organization.* — A

23 Lending Company shall be established only as a corporation; *Provided, That*
24 existing Lending Investors organized as single proprietorships or partnerships
25 shall be disallowed from engaging in the business of granting loans to the public
26 one (1) year after the date of effectivity of this Act.

1 No Lending Company shall conduct business unless granted an authority
2 to operate by the DTI.

3 **Section 5. Capital.** – The minimum paid-in capital of any Lending
4 Company which may be established after the effectivity of this Act shall be One
5 Million Pesos (P1,000,000.00); *Provided*, however, that Lending Companies
6 established and in operation prior thereto shall comply with the minimum
7 capitalization required under the provisions of this Section within such time as
8 may be prescribed by the DTI which time shall, in no case, be less than Three
9 (3) years from the date of effectivity of this Act and, *Provided*, further, that the
10 DTI may prescribe a higher minimum capitalization if warranted by
11 circumstances.

12 **Section 6. Citizenship Requirements.** — Upon the effectivity of this Act,
13 at least a majority of the voting capital stock shall be owned by citizens of the
14 Philippines.

15 The percentage of foreign-owned voting stock in any Lending Company
16 existing prior to the effectivity of this Act, if such percentage is in excess of 49%
17 of the voting stock, shall not be increased but may be reduced, and, once
18 reduced, shall not be increased thereafter beyond 49% of the voting stock of the
19 Lending Company. The percentage of foreign-owned voting stocks in any
20 Lending Company shall be determined by the citizenship of the individual
21 stockholders. In the case of corporations owning shares in a Lending Company,
22 the citizenship of the individual owners of voting stock in such corporations shall
23 be the basis in the computation of the percentage.

24 **Section 7. Amount and Charges on Loans.** — A Lending Company may
25 grant loans in such amounts and reasonable interest rates and charges as may
26 be agreed upon between the Lending Company and the Debtor. *Provided*, That
27 the agreement shall be in compliance with the provisions of RA 3765, otherwise

1 known as the Truth in Lending Act and Republic Act 7394, otherwise known as
2 the Consumer Act of the Philippines; and *Provided*, further, That the Monetary
3 Board, in consultation with the DTI and the industry, may prescribe such interest
4 rate as may be warranted by prevailing economic and social conditions.

5 **Section 8.** *Maintenance of Books of Accounts and Records.* — Every
6 Lending Company shall maintain books of accounts and records as may be
7 required by the DTI and prescribed by the Bureau of Internal Revenue and other
8 government agencies. In case a Lending Company engages in other businesses,
9 it shall maintain separate books of accounts for these businesses.

10 The Manual of Accounts prescribed by the BSP for lending investors shall
11 continue to be adopted by Lending Companies for uniform recording and
12 reporting of their operations, until a new Manual of Accounts shall have been
13 prescribed by the DTI.

14 It shall issue the appropriate instruments and documents to the parties
15 concerned to evidence its lending and borrowing transactions.

16 **Section 9.** *Authority of the DTI.* — The DTI is hereby authorized to:

- 17 a. Create a new division or bureau within its control to regulate and
18 supervise the operations and activities of Lending Companies in the
19 country.
- 20 b. Issue rules and regulations to implement the provisions contained
21 herein;
- 22 c. Issue rules and regulations on, among other things, minimum
23 capitalization, uses of funds received, method of marketing and
24 distribution, maturity of funds received, restrictions or outright
25 prohibition of purchases or sales of receivables with or without
26 recourse basis;

1 d. Require from Lending Companies reports of condition and such other
2 reports necessary to determine compliance with the provisions of this
3 Act;

4 e. Exercise visitorial powers whenever deemed necessary; and

5 f. Impose such administrative sanctions including suspension or
6 revocation of the Lending Company's authority to operate and the
7 imposition of fines for violations of this Act and regulations issued by
8 the DTI in pursuance thereto.

9 **Section 10. *Implementing Rules and Regulations.*** — Within six (6)
10 months after the approval of this Act, the DTI shall promulgate the necessary
11 rules and regulations implementing the provisions of this Act.

12 **Section 11. *Delineation of Authority between DTI and BSP.*** — Lending
13 companies shall be under the supervision and regulation of the DTI: *Provided,*
14 however, that Lending Companies which are subsidiaries and affiliates of banks
15 and quasi-banks shall be subject to BSP supervision and examination in
16 accordance with Republic Act No. 7653. *Provided,* further, That the Monetary
17 Board, after being satisfied that there is reasonable ground to believe that a
18 Lending Company is being used as a conduit by a bank, quasi-bank or their
19 subsidiary/affiliate to circumvent or violate BSP rules and regulations, may order
20 an examination of the Lending Company's books and accounts.

21 **Section 12. *Penalty.*** — A fine of not less than Ten Thousand Pesos
22 (P10,000.00) and not more than Fifty Thousand Pesos (P50,000.00) or
23 imprisonment of not less than six (6) months but not more than Ten (10) years
24 or both, at the discretion of the court, shall be imposed upon:

- 25 1. Any person who shall engage in the business of a Lending Company
26 without a validly subsisting authority to operate from the DTI.

- 1 2. The President, Treasurer and other officers of the corporation,
2 including the managing officer thereof, who shall knowingly and
3 willingly:
- 4 a. Engage in the business of a Lending Company without a validly
5 subsisting authority to operate from the DTI;
- 6 b. Hold themselves out to be a Lending Company, either through
7 advertisement in whatever form, whether in its stationery,
8 commercial paper, or other document, or through other
9 representations without authority;
- 10 c. Make use of a trade or firm name containing the words "*Lending*
11 *Company*" or "*Lending Investor*" or any other designation that
12 would give the public the impression that it is engaged in the
13 business of a Lending Company as defined in this Act without
14 authority; and
- 15 d. Violate the provisions of this Act.
- 16 3. Any officer, employee, or agent of a Lending Company who shall:
- 17 a. Knowingly and willingly make any statement in any application,
18 report, or document required to be filed under this Act, which
19 statement is false or misleading with respect to any material fact;
20 and
- 21 b. Overvalue or aid in overvaluing any security for the purpose of
22 influencing in any way the action of the company in any loan, or
23 discounting line.
- 24 4. Any officer, employee or examiner of the DTI directly charged with the
25 implementation of this Act or of other government agencies who shall
26 commit, connive, aid, or assist in the commission of acts enumerated
27 under Subsections 1 and 2 of this Section.

1 **Section 13. *Matters not covered by this Act.*** – The provisions of Republic
2 Act No. 3765, otherwise known as the “Truth in Lending Act”, Republic Act No.
3 7394 or the “Consumer Act of the Philippines” and other existing laws, insofar as
4 they are not in conflict with any provision of this Act, shall apply in matters not
5 otherwise specifically provided in this Act.

6 **Section 14. *Repealing Clause.*** – All laws, executive orders, letters of
7 instruction, rules and regulations, or provisions thereof which are inconsistent
8 with the provisions of this Act are hereby repealed, amended or modified
9 accordingly.

10 **Section 15. *Separability Clause.*** – If any portion hereof shall be held
11 invalid or unconstitutional, such invalidity or unconstitutionality shall not affect
12 the other provisions which shall remain in full force and effect.

13 **Section 16. *Effectivity.*** – This Act shall take effect fifteen (15) days after
14 its publication in at least two (2) national newspapers of general circulation.

15 Approved.

16

COMMITTEE ON BANKS, FINANCIAL INSTITUTIONS AND CURRENCIES

SUMMARY OF PROCEEDINGS

I. BACKGROUND

In the mid-70's, lending companies or lending investors emerged to address the financing needs of *common taos* who were left unserved by the more sophisticated forms of credit institutions. They provide credit services in areas where growth opportunities are abundant but restricted by lack of financial resources.

As of February 2005, there were about 10,885 lending investors. With the economic hardship driving people to avail of ready credit, the number of lending companies is expected to increase. Their huge number and their widespread distribution all over the country make lending companies an important segment of the financial sector.

Prior to the enactment of the New Central Bank Act (RA 7653), the Central Bank had authority over the lending companies¹. However, the New Central Bank Act removed the regulatory powers of the BSP over such companies.² In the absence of a specific law regulating lending investors and pursuant to DOJ Opinion No. 46 dated September 17, 2001, lending companies were placed under the regulatory power of the SEC.

In view of its regulatory powers, the SEC issued Memorandum Circular No. 13 (11 October 2001), which required:

- a. Lending Investors – to comply with the requirements of the **Financing Company Act of 1998**, its IRR and circulars relative thereto.
- b. Existing lending investors organized as partnerships or single proprietorships – to incorporate as financing companies with the following paid-up capital:

| Location | Minimum Paid-Up Capital | Period of Compliance |
|---|--------------------------------|---|
| Metro Manila and Other 1 st Class Cities | P 10 Million | Within three (3) years from effectivity of the Circular |
| Other Classes of Cities | P 5 Million | Within two (2) years from effectivity of the Circular |
| Municipalities | P 2.5 Million | Within one (1) year from effectivity of the Circular |

¹ In view of the CBP's mandated authority over the entire credit system.

² "Finance companies without quasi-banking functions" which are not subsidiaries/affiliates of banks or quasi banks were taken out of the regulatory powers of the BSP..

As of February 2005, only 360 lending investors have converted to finance companies and 81 applications for conversion were pending. The failure of the majority of lending investors to comply with Memorandum Circular No. 13 was mainly due to their inability to meet the high capitalization requirement. This Circular, which is currently suspended by the SEC, endangers the legitimate existence of Lending Companies.

Lending Companies, which failed to comply with the provisions of the Finance Company Act, were left without specific regulatory framework. The absence of adequate guidelines on the operations of these Lending Companies caused the proliferation of loan sharks which charge unconscionable interest rates. Moreover, this void made possible massive scams.

The passage of a law that will regulate the lending investors is essential for the continued operation of these companies and the protection of the general public.

II. COMMITTEE ACTION

- A. The Committee on Banks, Financial Institutions and Currencies (the "Committee") conducted a public hearing on the proposed bills on January 14, 2005.
- B. The discussions in the hearings, as well as the comments and suggestions in the position papers submitted to the Committee, were taken into consideration in the drafting of the Substitute Bill.

III. FINDINGS

- A. On the supervising agency

Discussion

There are differing opinions on the appropriate government agency that should govern the lending companies.

The BSP sees the Department of Trade and Industry (DTI) as the agency which has the capacity to regulate lending companies in view of the agency's wider network which will complement the widespread existence of the said companies all over the country.³ Moreover, lending companies are in the business of providing credit to the public which necessitates consumer protection. Unlike the deposit-taking institutions which are under the supervision of the BSP, the lending companies cannot borrow funds from the public. In this kind of business, what is needed is not the prudential-type of regulation⁴ but the consumer-protection type (which is geared primarily for the protection of the consumers – the borrowers). The BSP and the SEC are not the appropriate agencies to primarily provide consumer protection.⁵

³ Letter dated 29 October 2004.

⁴ This is applicable only in the supervision of deposit-taking institutions (e.g. banks and quasi-banks) for the protection of the public who provide credit to such institutions.

⁵ Assistant Governor Nestor Espenilla of the BSP.

The DTI, however, has reservations on the proposal to make it the regulatory body of lending companies on the ground that "Lending Companies are non-bank financial institutions extending credit facilities to consumers and enterprises, hence, (they are) under the authority of the SEC by virtue of RA 8556 or the Financing Company Act."⁶

Committee Consensus

Because of the wide distribution of DTI offices throughout the country, it has the capability of regulating lending companies. Moreover, the DTI was designated as the implementing agency of the Consumer Act⁷ on matters concerning consumer credit transactions.⁸

In view of the foregoing, the Committee agreed to put the lending companies under the supervision of the DTI to ensure the protection of the borrowers. In order for the DTI to effectively perform its duties under this proposed law, it shall be mandated to create a separate division for the supervision of lending companies.

B. On the form of organization

Discussion

The three bills require that a lending company shall be established only as a corporation. At present, there are about ten thousand (10,000) lending investors and yet around 53% operate as single proprietorship and 7% as partnership. The bills allow six months to one year allowance for these lending investors to incorporate.

Although some sectors are indifferent with respect to the form of organization, the SEC is adamant on requiring the incorporation of the lending investors for easy regulation. The incorporation of all the lending investors is one of the objectives of SEC's active support on the bills since most of the investment scams that it had caught were perpetrated by lending investors operating as single proprietorship.

Committee Consensus

In view of the difficulty in regulating lending investors operating as sole proprietorship or partnership, the Committee decided to require all lending investors to incorporate.

C. On the use of the term "microfinance"

Discussion

Senate Bill Nos. 1180 and 1762 define "lending company" as an entity primarily engaged in the business of microfinance by granting direct loans from their own funds or from other persons x x x."

⁶ DTI's Position Paper dated 3 February 2005.

⁷ Republic Act 7394, otherwise known as the Consumer Act of the Philippines

⁸ Article 6 of RA 7394 in relation to Title IV thereof.

The afore-quoted definition was opposed on the ground that the term "microfinance" is "applicable only to banks engaged in lending microfinance loan. Microfinance loan is defined under BSP Circular Nos. 272 and 273, dated 30 January and 27 February 2001."⁹

Committee Consensus

To avoid confusion, the Committee adopted the definition in SBN 1103, with certain revisions.

D. On the involvement of the DSWD in the promulgation of the IRR.

Discussion

Senate Bill Nos. 1180 and 1762 call for the involvement of the Department of Social Welfare and Development ("DSWD") in the promulgation of Implementing Rules and Regulations ("IRR"). BSP opined that the DSWD need not be involved in the promulgation of the IRR.¹⁰

Committee Consensus

The IRR will be promulgated by the DTI without DSWD's involvement.

⁹ BSP's Position Paper dated 29 October 2004.

¹⁰ Ibid.