REPUBLIC OF THE PHILIPPINES
DEPARTMENT OF FINANCE
INSURANCE COMMISSION
Insurance Commission Building
Manila

PROPOSAL FOR THE CORPORATE REHABILITATION OF NATIONAL LIFE INSURANCE COMPANY OF THE PHILIPPINES, INC. IN CONNECTION WITH THE CONSERVATORSHIP STATUS OF THE COMPANY UNDER SECTION 248 OF THE INSURANCE CODE (NOW SECTION 255 OF REPUBLIC ACT NO. 10607)

CRL Ref. No. 2013-002

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DIRECTIVE

08 November 2013

I. NATURE OF THE CASE

Before the Insurance Commission[1] are two (2) proposed Rehabilitation Plans for the restoration of the viability of National Life Insurance Company of the Philippines, Inc.[2]. The Rehabilitation Plans were submitted as a result of the conservatorship proceedings for National Life pursuant to Section 248 of the Insurance Code, now Section 255 of Republic Act No. 10607[3]. This Directive is being issued as a continuation of the said conservatorship process.

II. FACTS OF THE CASE

CIRCUMSTANCES LEADING TO CONSERVATORSHIP

As a result of the regular examinations being conducted on locally-operating insurance companies, it was noted that National Life was continuously suffering from Margin of Solvency deficiency. The Commission repeatedly

[1] Hereinafter referred to as "the Commission" for brevity
[2] Hereinafter referred to as "National Life" for brevity
[3] Hereinafter referred to as "New Insurance Code" for brevity

called the company's attention to address this problem and required it to make good the said deficiencies.

National Life attempted to solve the said deficiencies by infusing additional capital and by submitting supporting documents for certain assets to be admitted. Each time its Certificate of Authority (CA) was issued by the Commission, the deficiency of National Life was still manageable. In addition, the company was required to submit a sworn undertaking that it will comply with certain conditions within a certain period.

However, given the mounting deficiencies and despite the said courses of action taken by the company, it failed to show that the reissuance of a CA would not be detrimental to the welfare of the policyholders and the general public. Hence, after conducting the required due process, the Commission finally denied further issuance of a CA to National Life.

To determine whether the economic viability of the company can still be restored, the Commission decided to declare the company under conservatorship.

FIRST CONSERVATOR

On 19 August 2008, the Insurance Commission declared National Life under conservatorship for failure to comply with the solvency requirement pursuant to Section 194 of the Insurance Code. The company was ordered to cease and desist from taking in new risks of any kind and character.[4] Accordingly, Atty. Inocencio Ferrer Jr. was appointed by the Commission as National Life's first conservator.[5]

On 03 November 2008, the Commission lifted the order placing National Life under conservatorship and issued Certificate of Authority No. 2007-2008 upon the recommendation of the conservator and by reason of the corresponding undertakings executed by National Life.[6] The Certificate of Authority was subject to the following conditions, which must be complied with by National Life not later than 31 May 2009:

> "1. To make good the 2007 Margin of Solvency Deficiency of Php870 Million or whatever amount as may finally be determined on or before March 31, 2009;
> 2. Claims for whatever policyholders' benefits are due shall be given utmost priority;
> 3. To sell or dispose of major real estate properties on or before March 31, 2009; and

[4] Letter of the Commission to National Life dated 19 August 2008
[5] Letter of the Commission to Atty. Ferrer dated 19 August 2008
[6] Letter granting Certificate of Authority dated 03 November 2008

4. To submit to this Commission a progress report on the disposition of the real estate properties on a monthly basis."[7]

As a result, National Life was allowed to continue operating its insurance business. A subsequent examination, however, of its 2007 financial condition showed that National Life again failed to address its capital impairment of Php118,268,967.99 and Margin of Solvency deficiency amounting to Php850,337,744.76.

In 2009, the company informed the Commission that several investors were interested to infuse additional capital to rehabilitate the company. In light of this development, the Commission renewed the license of the company with the following conditions:

"1. A monthly status report shall be submitted regarding any development that may arise out of its engagement with x x x;[8]

2. Additional Capital shall be infused on or before December 31, 2009 in compliance with the Commission's Advisory on Implementation of Department Order 27-06; and

3. The deficiency in Capital Impairment and Margin of Solvency in the amount of P850,337,744.76 or whatever remaining deficiency pertaining to 2007 Annual Statement shall be fully covered up on or before March 31, 2010."[9]

In the same year, the Margin of Solvency deficiency in the 2007 Annual Statement was further reduced to Php750,258,420.39 after considering as admitted asset the company's real estate of Php8,438,376.78, together with several afterdate transactions totalling Php85,593,150.42.

2010 CEASE AND DESIST ORDER

Failing to make good its capital impairment and Margin of Solvency deficiency in the amount of P750,258,420.39 as of 31 December 2007, National Life was placed under conservatorship by the Commission and appointed Mr. Merton V. Deveza as the second conservator of National Life on 31 March 2010.[10] On 05 April 2010, the Commission issued a Cease and Desist Order.[11] However, Mr. Deveza was immediately replaced by the Officer-in-Charge of the Conservatorship, Receivership and Liquidation Division, Atty. John Apatan, as the *Ex-Officio* Conservator on 14 April 2010.[12]

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[7] *Id*

[8] The name of the investor is being withheld pending approval

[9] Letter of the Commission to National Life dated 26 November 2009

[10] Letter of the Commission to National Life dated 31 March 2010

[11] Letter of the Commission to National Life dated 05 April 2010

[12] Letter of the Commission to National Life dated 14 April 2010

Thereafter, another examination conducted by the Commission revealed that National Life had Margin of Solvency deficiency of Php416,345,330.40 as of 31 December 2008[13] and that its paid-up capital of Php100,000,000.00 was impaired by Php440,845,330.41 such that the minimum required net worth of Php100,000.000.00 under Department Order No. 27-06 was not complied with.[14] However, the company's request for reconsideration of certain accounts was granted thereby reducing the capital impairment and margin of solvency deficiency to Php147,496,212.82 and Php171,996,212.82, respectively.

2010 CONDITIONAL CERTIFICATE OF AUTHORITY

Sometime in May 2010, Mr. Benjamin L. De Leon, President and Chief Executive Officer of National Life, informed the Commission of the potential acquisition of National Life by another corporation. Further, the existing stockholders paid an aggregate amount of Fifty Million Pesos (Php50,000,000.00), which was treated as deposit for future stock subscription. To provide an opportunity for the potential acquisition and considering the additional cash infusion made by the stockholders, the Commission issued a Conditional Certificate of Authority for National Life to operate for the licensing period ending 30 June 2010.

2010 CONSERVATORSHIP

The additional Fifty Million Pesos cash infusion, however, proved to be inadequate to improve the financial viability of National Life for a sustainable period. In addition, no concrete development was presented concerning the proposed acquisition of the company. Thus, on 09 September 2010, National Life was again declared and placed under conservatorship by the Commission.[15] This time, Ms. Marichu T. Celi was appointed by the Commission as the third conservator for National Life.

2011 PROPOSED REHABILITATION

On 26 January 2011, the conservator submitted to the Commission a Rehabilitation Plan[16] for National Life. One of the provisions of this Plan was for the reduction of the interest rate on the Premium Deposit Fund from four percent (4%) to two percent (2%) per annum. On 08 June 2011, the Insurance Commission approved the said interest reduction, but deferred the approval of the entire Rehabilitation Plan.

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[13] Memorandum of FED II to the Insurance Commissioner dated 20 May 2010

[14] *Id*

[15] Letter of the Commission to National Life dated 09 September 2010

[16] 2011 Rehabilitation Plan

In the meantime, Ms. Celi took a leave as conservator effective 31 May 2011. Accordingly, the Commission appointed Atty. Clifford Chua as the fourth conservator.[17]

2011 REVISED REHABILITATION PLAN

A Revised Rehabilitation Plan was formulated by the conservator which was approved by the Commission on 14 September 2011. One of the key components of the plan was the additional cash infusion of Four Hundred Four Million Pesos (PhP404,000,000.00) payable as follows:

Amount	When Payable
Php 104,000,000.00	Upon approval of the Rehabilitation Plan
100,000,000.00	After the first year of operations
100,000,000.00	After the second year of operations
100,000,000.00	After the third year of operations

The first infusion of PhP104 Million was subsequently rescheduled as follows:

Amount	When Payable
Php 50,000,000.00	Not later than 20 October 2011
Php 54,000,000.00	Not later than 31 December 2011

Based on the Revised Rehabilitation Plan, the Commission will issue a Certificate of Authority in favor of National Life only upon compliance with the requirements stated in the plan.

To ensure National Life's compliance with its undertaking under the Revised Rehabilitation Plan, the Commission, in a letter dated 12 December 2011, reiterated that the Commission would issue a Certificate of Authority upon compliance with the following conditions:

> "1. Infusion of P104Million on or before 15 December 2011; and
>
> 2. Conformity with the Rehabilitation Plan and undertaking to comply with the timelines set forth in the Rehabilitation Plan, including but not limited to the following:
>
> a. Infusion of P100Million per annum on or before the 31st of October each year from 2012 up until 2014;
> b. Compliance with the Manual on Corporate Governance;
> c. Timely submission of the documents and reports as may be required by the Commission; and
> d. Reorganization of Top Management with the approval of the Commission."[18]

[17] Letter of the Commission to National Life dated 16 June 2011

In compliance therewith, National Life paid the Php104,000,000.00 first tranche cash infusion.

In addition, the Commission formed a Crisis Team on 13 December 2011in order to monitor and resolve issues concerning National Life.[19]

Accordingly, on 06 February 2012, the Commission issued a Conditional Certificate of Authority in favor of National Life granting it the privilege to continue marketing its existing insurance products to existing policyholders.[20] One of the conditions therein was for National Life to infuse additional cash in the amount of Php100 Million not later than 20 October 2012.

However, based on the 2010 annual statement, it was discovered that National Life sustained a Margin of Solvency deficiency of Php2,533,829,944.99 even after applying the initial cash infusion of Php104,000,000.00.[21] Hence, National Life was again declared under conservatorship.

On 30 March 2012, Atty. Senen Y. Glinoga was appointed as the fifth conservator of National Life and was thereafter replaced upon the appointment of Atty. John Apatan as *ex officio* conservator on 17 December 2012.

2013 CONSERVATOR'S PROPOSAL

On 22 January 2013, the Commission appointed Mr. Ermilando D. Napa to replace Atty. Apatan as National Life's sixth conservator.[22] To date, Mr. Napa remains to be the conservator of National Life.

In the performance of his duty as conservator, Mr. Napa prepared and presented to the Commission a new Proposed Rehabilitation Plan dated 12 March 2013 ("2013 Conservator's Proposal" for brevity).

The 2013 Conservator's Proposal is basically characterized as a **Debt-to-Equity Conversion**. Its aim is "to immediately improve NLIC's capital and liquidity positions, reduce debts to manageable levels and, accordingly allow it to immediately resume business operations efficiently and eventually achieve, in at most ten (10) years, sustainable growth and profitability."[23] The main components of the 2013 Conservator's Proposal are as follows:

> "1. Conversion into Common Shares of NLIC of the following Debts/ Account:
>
> 1.1. Premium Deposit Fund

[18] Letter of the Commission to National Life dated 12 December 2011
[19] Office Order No. 200-2011 dated 13 December 2011
[20] Certificate of Authority dated 06 February 2012
[21] Memorandum of FED II to the Insurance Commissioner dated 30 April 2012
[22] Letter of the Commission to National Life dated 22 January 2013
[23] P. 1, 2013 Conservator's Plan

1.2. Loans from Related Parties
1.3. Agency Retirement Fund
1.4. Advances from Shareholders and Related Parties
1.5. Deposit for Future Subscription Account

2. Orderly disposition of the real estate investments and, in particular, immediate sale of the NLIC Building at Ayala Avenue, Makati City (NLIC-Ayala Bldg.)

3. Repayment of Loans from Banco de Oro Unibank, Inc. (BDO) and Philippine Business Bank (PBB)

4. Quasi-Reorganization of NLIC

5. Proper Management of Investment Portfolio for optimum yield

6. Aggressive collection of long outstanding loans receivable

7. Development and launching of new competitive products duly Approved by IC

8. Strengthening of NLIC's organizational structure and the underlying management team

9. Rationalization of operating and administrative policies, system procedures and related internal control

10. Redemption of unprofitable and/or non-sustainable life insurance

11. Rebuilding the Company's name and image in the market."

POLICYHOLDERS' PROPOSAL

From 11 April to 07 June 2013, the Commission conducted a series of consultation meetings with all interested parties to discuss the 2013 Conservator's Proposal. A group of policyholders, premium deposit fund holders, and agents of National Life led by Ms. Katherine Yupangco, actively participated in the discussions and thereafter submitted to the Commission a letter[24] containing their collective proposal for the rehabilitation of National Life entitled **"Proper Conservatorship-Receivership for the Sole Purpose of Rehabilitation Plan"[25]**.

The Commission formed an evaluation team, which was directed to come up with its own independent assessment of the proposals and counter-proposals, taking into account all the submissions discussed above.

Through a letter dated 25 July 2013, sent via e-mail dated 26 July 2013, the same group of policyholders formally requested the Commission to recognize their "participatory rights". They specifically requested that they be allowed to participate "in the decision-making process in NLIC's

[24] Letter to the Commission dated 20 May 2013
[25] Hereinafter referred to as "Policyholders' Proposal" for brevity

operations, pending your approval of a viable rehabilitation plan acceptable to all stakeholders."

Upon further clarification, however, it became clear that the policyholders wanted to participate in evaluating the 2013 Conservator's Proposal and in presenting their own rehabilitation plan. For that reason, the Commission granted the request of the policyholders and thereafter conducted a series of meetings with them in evaluating the 2013 Conservator's Proposal and in reviewing their proposed rehabilitation plan. The first of these meetings was held on 31 July 2013 where the policyholders discussed their suggestions on the conservator's rehabilitation plan for National Life.

On 06 August 2013, the group of policyholders presented their own rehabilitation plan before the Commission. The parties agreed that the said Policyholders' Proposal shall undergo actuarial study.

Subsequently, the policyholders submitted the final version of the Policyholders' Proposal dated 19 August 2013. Based on the said final version, the rehabilitation of the National Life would be implemented in the following manner:

> "1. Sale of NLIC Ayala building in 2013 with gain, after tax, of P390 million
>
> "2. Bank loans payment of P700 MILLION pesos upon sale of NLIC Ayala building
>
> "3. Monthly principal payment of PDF @ 2% p.a. (from 2H 2013 to end 2017). Discontinue interest payment for PDF P1 million & above.
>
> "4. Policyholders' PDF, Agents' Service Fee (SF) and Employees' Retirement Fund (RF):
>
> > 15% Conversion to insurance premium in 2H 2013, incl. due for 2013
> > 65% Conversion to equity at end 2017
> > 20% Pay out in 3Q 2018, net of payments in item (3)
>
> "5. Though on the aggregate the mix is 15%/65%/20%, the approach of the plan for the PDF is based on "Socialized Calibration," as follows:
>
> > >PDF balance <P100k - 100% converted to insurance premiums
> > >PDF balance P100k & above - 7% insurance/71% equity/22% cash
>
> "6. Gross Premiums to be generated via new IC license (issued upon approval of the plan), as follows:
>
> > P84Mn-2014, P200Mn-2005, P356Mn-2016, P542Mn-2017, & P758Mn-2018, aggregating P940Mn for 5 years (2014-2018) by fully trained sales force of 140 agents
> >
> > Year-to-year increase of First year gross premiums of 49%, 38%, 25%, & 20%.

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Including "Proposal for Micro-insurance Products, and accreditation to offer the Compulsory Insurance Coverage for Agency Hired Workers pursuant to AMWA-RA10022 Section 23 (37-A of RA 8042)"

"7. Existing Business: All renewals and no new applications
Aside from renewals by the PDF holders and sales agents of their existing insurance policies, targeted gross premiums for the existing business are -

2013 - P56 Mn
2014 - 40
2015 - 34
2016 - 31
2017 - 30
2018 - 25
Total - P216 Mn

"8. Stockholders' Equity

Negative Stockholders' Equity, 12/31/2012.........	**(P2,129.65 Mn)**
Loans/P to related parties and Advances from subs. offset vs capital deficiency............	102.93
Negative Stockholders' Equity after offset.........	(P2,026.72 Mn)
Capital build-up:	
PDF/Agents' SF/Employees' RF conversion to equity (14,232,600 shares)...............	1,423.26
Income from new business via new IC license...	269.48
Gain on sale of Ayala building.....................	390.00
Income from existing business, incl. conversion of PDF/	
Targeted Positive Stockholders Equity, 12/31/2018..............................	**P56.02 Mn**
Book value/share, 12/31/2018	**P 3.94**

*Note: Capital re-structuring at end - 2018

"9. Annual Cash Flow

Net receipts for 2013.........................P941 Mn
Net disbursements for 2014................ (372)
Net receipts for 2015.........................60
Net receipts for 2016.........................142
Net receipts for 2017.........................288
Net receipts for 2018.........................193
Aggregate net receipts for 6 years......P1,252 Mn

"10. Optimal investment of net funds generated
> Year-end cash levels-

2013 - P951 Mn
2014 - 579
2015 - 638
2016 - 781
2017 - 1,069
2018 - 1,262
Average - P880 Mn

> With the above figures, around P860 million on the average are investible.
> The yield on invested funds is targeted at 4%p.a., gross of tax

"11. Overhead Cost-Cutting

>Manpower headcount staggered reduction
Salaries & wages: cut by 40%
Management Team professional fees: 15% up at the start w/ 15% annual increase

>Steady decrease in other general & administrative expenses"

A series of meetings and deliberations were conducted among the representatives of the Commission, the Conservator, policyholder representatives and National Life President Benjamin De Leon, which culminated on 02 September 2013. After the said final deliberation, National Life and the group of policyholders were required to prepare their respective memoranda on the arguments and issues raised during the said meeting and to submit the same on or before 06 September 2013.

Accordingly, National Life President De Leon submitted its Memorandum dated 06 September 2013 containing arguments in favor of the 2013 Conservator's Proposal and against the Policyholders' Proposal.

In a letter dated 07 September 2013, the group of policyholders, through their counsel, Atty. Joseph Migriño, requested additional time to file their Memorandum. Notwithstanding the late request, the Commission issued a letter granting the same and allowed them to submit their memorandum on or before 16 September 2013.

The group of policyholders submitted their Memorandum dated 16 September 2013. In the said memorandum, they reiterated their arguments against the 2013 Rehabilitation Plan as proposed by the conservator and highlighted the merits of the Policyholders' Proposal.

Thereafter, the Evaluation Team assessed the 2013 Conservator's Proposal and the Policyholders' Proposal and submitted its recommendation to the Insurance Commissioner for his consideration.

III. DISCUSSION OF EACH PROPOSAL

POLICYHOLDERS' PROPOSAL

Similar to the 2013 Conservator's Proposal, the Policyholders' Proposal, does not involve an outright infusion of sufficient capital. It intends to improve the financial standing of National Life through the sale of real property, and conversion of the Premium Deposit Fund (PDF), Service Fee (SF) of agents and Retirement Fund (RF) of employees as set out below. It likewise prays for the issuance of a new Certificate of Authority from the Commission.

As elucidated in their Memorandum, dated 16 September 2013, the company's building along Ayala Avenue, Makati City shall be immediately sold upon approval of their proposal. This is "to provide liquidity and payment of secured bank loans to prevent foreclosure and to maximize sale price".[26]

The proposal involves the conversion of the PDF, SF and RF. The PDF will be converted through "socialized calibration", where the type of conversion will be dependent on the amount of PDF involved. If the PDF balance is less than Php100,000.00, 100% of this will be converted to insurance premium. If the same is Php100,000.00 and above, the same will be converted in the following proportion: 7% insurance premium, 71% equity and 22% cash. On the other hand, the SF of agents and RF of employees will be converted as follows: 15% insurance, 65% equity and 20% cash.

The proposal presupposes that the Commission would immediately issue a Certificate of Authority or license to sell the approved insurance products of National Life. Consequently, the company is projected to generate premium income from its authorized operation.

The proposal also recommends the immediate and drastic cost reduction measures such as the removal of all existing directors, and excess management personnel and staff. A governance board will also be created that will monitor and evaluate the appointed rehabilitator.

While the Policyholders' Proposal presents an earnest intention to rehabilitate National Life, the proposal suffers from several legal and practical issues.

At the outset, it will be observed that the proposal is anchored on the assumption that the Commission will issue a Certificate of Authority or license to sell in favor of National Life **notwithstanding its deficiency in the capital and net worth requirement.** Section 188 of the Insurance Code (now Section 194 of the New Insurance Code) requires that in order to engage in business, an insurance company shall, in a stock corporation, possess a paid-up capital equal to at least One Billion Pesos (P1,000,000,000.00) and that a domestic insurance company already doing business in the Philippines shall have a net worth by 30 June 2013 of Two Hundred Fifty Million Pesos (P250,000,000.00). Failure to comply with such capital and net worth requirement prevents the issuance of Certificate of Authority to engage in the insurance business in the Philippines.

Based on its 2011 audited financial statements, National Life has a capital deficiency of Php2.101 billion and such condition continues to persist. In fact, based on the projected stockholder's equity under the Policyholders' Proposal, National Life will continue to have negative equity

[26]Memorandum of policyholders dated 16 September 2013

from 2013 to 2017 and attain a positive equity of Php56.02 million only by 2018.[27] Since the company cannot comply with the net worth requirement as provided for under Section 194 of the New Insurance Code during the expected period of rehabilitation from 2013 to 2018, **the Commission is not authorized to issue a Certificate of Authority.** Consequently, without such authorization, the company cannot legally operate. Moreover, the shares of stock of policyholders will not be attractive to any strategic investor.

Needless to mention, without such Certificate of Authority, the entire Policyholders' Proposal will have no legal foundation to stand on and thus will ultimately falter. Hence, on the basis of this legal obstacle alone, the Policyholders' Proposal must be rejected.

Related to the above legal predicament is the financial issue of projected target amount of premiums to be generated from new businesses as presented by the Policyholders' Proposal. The success of the plan hinges on the supposition that National Life will generate Php1.940 billion as accumulated annual gross premium on new applications from 2014 to 2018, broken down as follows:

Year	**Target Annual Gross Premium on New Applications**
2014	Php 84 million
2015	Php 200 million
2016	Php 356 million
2017	Php 542 million
2018	Php 758 million
Total	**Php 1,940 million**

Upon careful assessment, we are convinced that **the Policyholders' Proposal does not support the above figures.** The attainment of the projected premium income is highly improbable considering that National Life, if given the Certificate of Authority, can only sell two (2) types of products, namely, Ordinary Life and 20-Pay Life, both of which are traditional plans. Under the existing business environment, such traditional products are not that attractive because of the prevailing low interest rates. In addition, the success of its operations is still uncertain since it lacks a client base especially so as the company suffers from a negative public perception. National Life needs a strategic partner with a marketable name to re-establish its reputation, reposition its insurance brand, and bolster its marketing force.

Therefore, assuming *arguendo* that the Commission can issue a new Certificate of Authority to National Life, the possibility of achieving the target gross premiums is **highly doubtful**.

27 Page 31, Policyholders' Proposal dated 19 August 2013

Another issue is the repercussion of partial and selective conversion of PDFs. The Policyholders' Proposal requires the conversion of the PDF based on "socialized calibration". It means that an individual premium deposit that is less than Php100,000.00 will be totally converted to insurance premium. However, if the PDF is Php100,000.00 and above, it will be converted based on the following proportion: 7% insurance premium, 71% equity and 22% cash.

By instituting such "socialized calibration", it will effectively create distinctions between policyholders having PDF with less than Php100,000.00 and those with Php100,000.00 and above. Such classification violates the principles of equal treatment and fair play.

However, the Commission finds some merits in the Policyholders' Proposal, which will be shown in the dispositive portion of this Directive.

2013 CONSERVATOR'S PROPOSAL

The 2013 Conservator's Proposal is anchored on the conversion of debts and accounts amounting to Php2.42 billion[28], including 100% of the PDF amounting to Php2.08 billion[29], to equity instead of infusing additional amount of capital by existing shareholders of the company or by a third party investor. The objective of such conversion is to substantially improve the capital of National Life **from a negative net worth of Php2.1 billion**[30] **to a positive net worth of Php134 million**.

Thereafter, the office building of National Life along Ayala Avenue, Makati City is proposed to be sold for Php1.6 billion or higher, net of value added tax. This is intended to immediately improve the liquidity position of the company and **further increase its equity from Php133.91 million to Php524 million.**

The 2013 Conservator's Proposal also aims to address the Php2 billion[31] financial deficiency and required risk-based capital ratio through a proposed quasi-reorganization of National Life. The proposal will reduce the par value of its outstanding share capital from Php100 par value to Php20 par value without increasing the number of outstanding shares.

The 2013 Conservator's Proposal, being an innovative mode of rehabilitating an insurance company, must pass the crucibles of legality and economic viability. Accordingly, important legal observations and critical financial analyses should be discussed.

Based on the five-year financial projection of the 2013 Conservator's Proposal dated 30 May 2013, the projected premium income for new

[28] Rounded off
[29] *Id*
[30] *Id*
[31] *Id*

business appears to be optimistic. The proposal projected the following premium income:

Year	Projected New Income from New Business
1st year	Php8 million
2nd year	Php23.4 million
3rd year	Php28.08 million
4th year	Php33.696 million
5th year	Php40.435 million
Total	**Php133.611 million**

While the projected Php8 million premium income for the first year is reasonable, the succeeding projections have practicability concerns. It must be emphasized that the projected premium income sales of National Life will only come from two approved life insurance products, namely, Ordinary Life and 20-pay Life Plans, which are both traditional and the kinds of which are offered by many other, more stable life insurance companies. While National Life submitted to the Commission additional insurance products for its approval, namely: Single Pay Whole Life, 5-Pay Whole Life, 10-Pay Whole Life and 15-Pay Whole Life Plans, they need to review the actuarial assumptions in light of the declining interest rates and resubmit the same for the Commission's consideration and approval. Furthermore, the success in achieving the projected premium income is largely dependent on the support of agents and their capability to meet the high premium production targets.

The viability of the 2013 Conservator's Proposal is highly dependent on the 100% conversion of debt-to-equity. The proposed debts and accounts to be converted into equity based on the 2012 unaudited financial statements of National Life amount to Php2.4 billion[32]. **The successful conversion of the said debts and accounts will result to an immediate improvement of the company's net worth from a negative Php2.1 billion[33] to a positive Php134 million.** Hence, this will improve the capital and liquidity position of the company and subsequently operate in an economically feasible manner to the benefit of its policyholders and creditors.

The debt-to-equity conversion is given great consideration in light of the stockholders' failure to infuse additional capital. Since there is no intention on the part of the stockholders of National Life to further infuse additional capital or to submit an infusion plan to cure the company's huge financial deficiencies, it is now very clear that National Life will remain insolvent and will not be palatable to strategic investors if no drastic move is to be undertaken, such as the conversion of liabilities to capital.

[32] *Id*
[33] *Id*

We take note that based on the Conservator's Report dated 19 June 2013 and available records, only 375 out of 8,864 PDF holders have signified their support to the 2013 Conservator's Proposal. It means that only 4.2% agrees with the plan, which is equivalent to only Php298.6 million out of Php2.126 billion PDF (14%) based on the 2011 audited financial statements. Nevertheless, the said conservator's report states that "some PDF holders are still in a wait-and-see attitude, believing that IC will anyway compel the debt-to-equity conversion, x x x should IC decides (*sic*) to finally approve the REHAB PLAN".

The Commission deems it necessary to adopt an innovative mode of rehabilitation in order to help an ailing insurance company operate back to its financial health.

Due to the more realistic prospect of the debt-to-equity conversion, the Commission may approve the same pursuant to its authority under section 255 of the New Insurance Code. The said provision of law specifically authorizes the Insurance Commissioner to grant the conservator "all powers necessary to preserve the assets of said company, reorganize the management thereof, and **restore its viability**" and "such other powers as the Commissioner shall deem necessary". This comprehensive authority is granted by law to enable the conservator, under the direct supervision of the Commissioner, to effectively improve the solvency and liquidity position of the company. Clearly, the option of debt-to-equity conversion may be validly approved by the Commission even in the absence of the unanimous consent of affected creditors. The consent of the creditors has been effectively substituted by the law.

Furthermore, conservatorship is in the nature of rehabilitation proceedings[34]. Hence, laws and regulations concerning corporate rehabilitation will also apply suppletorily. Related laws provide supportive guide as to the propriety of allowing reasonable rehabilitation plan without the consent of affected creditors and policyholders. These laws include (1) Republic Act No 10142 or the Financial Rehabilitation and Insolvency Act of 2010 ("FRIA" for brevity), (2) Interim Rules of Procedure on Corporate Rehabilitation[35] ("IRPCR" for brevity), and (3) Rules of Procedure on Corporate Rehabilitation[36] ("RPCR" for brevity).

In fact, Section 64 of the FRIA[37] permits a rehabilitation court to approve a rehabilitation plan despite the rejection of creditors, so long as the enumerated safeguards are complied with.

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[34] *Republic of the Philippines vs. del Monte Motors* (G.R. 156956, 09 October 2006)

[35] A.M. No. 00-8-10-SC, 21 November 2000

[36] A.M. No. 00-8-10-SC, 02 December 2008

[37] Section 64. Creditor Approval of Rehabilitation Plan. - The rehabilitation receiver shall notify the creditors and stakeholders that the Plan is ready for their examination. Within twenty (20) days from the said notification, the rehabilitation receiver shall convene the creditors, either as a whole or per class, for purposes of voting on the approval of the Plan. The Plan shall be deemed rejected unless approved by all classes of creditors whose rights are adversely modified or affected by the Plan. For purposes of this section, the Plan is deemed to have been approved by a class of creditors if members of the said class

LIQUIDATION OPTION

National Life was placed under conservatorship pursuant to Section 248 of the Insurance Code, now Section 255 of the New Insurance Code. Due to its continued insolvency and in the absence of an approved and viable rehabilitation plan, the company may be placed under liquidation as provided under Section 249 of the Insurance Code, now Section 256 of the New Insurance Code.

In case of involuntary insolvency, the unsecured creditors, such as PDF holders, will only receive approximately seven percent (7%) of their respective investment. This is based on the computation attached as Annex "A" in the 2013 Conservator's Proposal dated 12 March 2013 to which the Commission concurs. With this repercussion in mind, **rehabilitation provides a better option** for the said unsecured creditors of National Life.

IV. DECISION

In the light of better prospects under rehabilitation, the Commission rules out the liquidation of National Life. **Upon careful evaluation of the Policyholders' Proposal and the 2013 Conservator's Proposal, it becomes evident that the rehabilitation of National Life may be effected by adopting the salient elements of both proposals.** Furthermore, important additions and modifications must be made to provide safeguards to the rights of the policyholders and other stakeholders.

1. The following components of the 2013 Conservator's Proposal are hereby approved:

   a. National Life's (a) premium deposit fund, (b) loans from related parties, (c) agency retirement fund, (d) advances from shareholders and related parties and (e) deposit for future subscription account will be converted into common shares of the said company.
   b. Repayment of Loans from Banco de Oro Unibank, Inc. (BDO) and Philippine Business Bank (PBB).
   c. Proper Management of Investment Portfolio for optimum yield.
   d. Aggressive collection of long outstanding loans receivables.

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holding more than fifty percent (50%) of the total claims of the said class vote in favor of the Plan. The votes of the creditors shall be based solely on the amount of their respective claims based on the registry of claims submitted by the rehabilitation receiver pursuant to Section 44 hereof.
Notwithstanding the rejection of the Rehabilitation Plan, the court may confirm the Rehabilitation Plan if all of the following circumstances are present:
(a)The Rehabilitation Plan complies with the requirements specified in this Act.
(b) The rehabilitation receiver recommends the confirmation of the Rehabilitation Plan;
(c) The shareholders, owners or partners of the juridical debtor lose at least their controlling interest as a result of the Rehabilitation Plan; and
(d) The Rehabilitation Plan would likely provide the objecting class of creditors with compensation which has a net present value greater than that which they would have received if the debtor were under liquidation.
(See also Section 11, Rule 4 of RPCR and Section 23, Rule 4 of the IRPCR)

e. Development and launching of new competitive products duly approved by Commission.
f. Strengthening of National Life's organizational structure and the underlying management team.
g. Rationalization of operating and administrative policies, system procedures and related internal control.
h. Redemption of unprofitable and/or non-sustainable life insurance.
i. Rebuilding the company's name and image in the market.

Note that except for paragraphs 1a and 1h, all the above items are also contained in the Policyholders' Proposal.

It must be clarified that the above components must be viewed with the understanding that the specific process or procedure in the implementation of the same must be approved by the Commission and subject to the requirements of the Securities and Exchange Commission (SEC) and other concerned government agencies.

2. The Commission approves the sale of real estate properties including the National Life Building along Ayala Avenue, Makati City, which was contained in both proposals.

3. Supplementary to the above components, the National Life must comply with the following conditions:

a. The minimum net worth requirement of Php250 million under Section 194 of the New Insurance Code.

Based on the 2013 Conservator's Proposal, the conversion of debt-to-equity will result to a positive net worth of Php134 million. Hence, the company will still be short of Php116 million in required net worth. In order to achieve the net worth requirement, National Life may either (1) infuse additional capital of Php116 million, or (2) immediately sell its real property at a price that will produce a net gain of at least Php116 million. The implementation of the said options must be with the prior approval of the Commission and subject to the requirements of SEC and other concerned government agencies. National Life must also comply with risk-based capital requirement under the New Insurance Code once the Commission issues its implementing circular on the matter.

b. The creation of an Interim Governance Board and the subsequent reconstitution of the Board of Directors.

As provided under the Policyholders' Proposal, an Interim Governance Board ("IG Board" for brevity) composed of seven (7) members shall be created within fifteen (15) days from the issuance of this Directive. The primary role of the board shall be to monitor the general operations of the company, and its membership will be composed of the following:

a. 2 representatives from the policyholders;
b. 1 representative from National Life;
c. 1 representative from corporate creditors;
d. A Chairman of the IG Board, to be appointed by the Insurance Commissioner from the private sector; and
e. Deputy Commissioner for Financial Examination and Deputy Commissioner for Legal as *ex officio* representatives from the Commission.

All the members of the IG Board shall be appointed by the Commissioner. All actions of the IG Board shall be subject to the final approval of the Commissioner. The IG Board shall submit their specific functions and processes for the evaluation and approval of the Commissioner. The Conservator shall continue to exercise his functions during the operation of the IG Board.

The existence of the IG Board shall automatically cease upon the reconstitution of the Board of Directors ("BOD" for brevity), which shall be composed of nine (9) members, namely:

1. Five (5) directors representing the converted shares pertaining to the PDF and Agency Retirement Fund;
2. One (1) director representing the existing shareholders and the converted loans/advances from related parties;
3. Three (3) independent directors appointed by the Commissioner; and
4. A Chairman of the Board appointed by the Commissioner, from the private sector.

c. The conservatorship will continue until the company fully complies with the minimum net worth requirement and unimpaired paid-up capital under Section 194 of the New Insurance Code, which should not be later than 6 months from the date of issuance of this Directive.

The process of conservatorship will continue until National Life can show its compliance with (1) the required net worth of Php250 million and (2) the necessary non-impairment status of its capital under Section 194 of the New Insurance Code, which should not be later than six (6) months from the date of issuance of this Directive.

The 2013 Conservator's Proposal shows that after the debt-to-equity conversion, National Life will still have net worth deficiency of Php116 million. To remedy this, the building of National Life along Ayala Avenue, Makati City will be sold. However, notwithstanding the conversion and sale, the paid-up capital will still be impaired to the extent of Php1.993 Billion. Based on the proposal, this will be remedied by the company undergoing quasi-reorganization. Therefore, the company's debt-to-equity conversion program and quasi-reorganization are indispensable requirements for the issuance of a Certificate of Authority.

The company shall be given up to six (6) months from the date of issuance of this Directive to accomplish the said goals. After the six month period, the Commission will evaluate the rehabilitation of National Life and issue a corresponding Directive. The company will continue to be under the close supervision of the Commission even if conservatorship ceases due to the improvement of its business until the Commission gains confidence that the company could already run its operations normally.

d. The Commission's acceptance of a qualified strategic investor as a condition for the finalization of debt-to-equity conversion.

The Commission recognizes the fear of the policyholders which they expressed repeatedly during previous meetings that in case no strategic investor comes in after they have converted their PDF into shares of stock, their PDF will have no value at all. To ward off this apprehension, we rule that the final legal conversion step (i.e., the signing and submission of the enabling documents, waivers, special power of attorney, deeds of assignment, proxies, etc.) should not be undertaken until the negotiation with and the consequent final offer of the strategic investor, become concrete to the extent that it can already be implemented simultaneously with the signing of the final conversion documents by the PDF holders and creditors.

Hence, while this Directive already authorizes the 100% debt-to-equity conversion, the final steps will be subject to the consideration and approval of the Commission. In relation thereto, the legal process of converting debt-to-equity with the SEC will be finalized only after the Commission determines and confirms the existence of a legitimate strategic investor. In order to be considered legitimate, the strategic investor must be compliant with the "fit and proper" rule under the Insurance Code[38] and the provisions of the Anti-Money Laundering Act, and must present a viable and reasonable business proposal approved by the Commission. The Commission, National Life, policyholder representatives, and the strategic investor will enter into a Memorandum of Understanding embodying the particular provisions of the sale of the converted shares to the strategic investor. The same shall be subject to the final approval of the Commission.

We are convinced that the foregoing **Modified Rehabilitation Plan is the more viable and advantageous option.**

WHEREFORE, in addition to the foregoing, the Conservator is hereby directed to:

[38] Section 193, New Insurance Code

1) Proceed with the **finalization and execution of the Rehabilitation Plan** as modified in this Directive. The Final Rehabilitation Plan and its attachments (i.e. audited financial statements, updated policyholder list, property selling guideline and procedure, timeline, and other supporting schedules) shall be submitted to this Commission within thirty (30) days from the issuance of this Directive. With the prior approval of the Insurance Commission, the Final Rehabilitation Plan shall be supplemented or amended from time to time to address changing conditions;

2) Continue to submit **monthly operational and financial reports** to the Commission;

3) Set in motion the negotiation with **a strategic investor** in accordance with the terms of this Directive; and

4) Ensure that the building blocks of the approved rehabilitation plan [i.e. debt-to-equity conversion (to improve the net worth), sale of the major real estate properties (to improve liquidity and comply with the minimum capitalization), and quasi-reorganization (to remedy the capital impairment and comply with the risk-based capital requirement)] are accomplished within six (6) months from the issuance of this Directive.

As mentioned during the consultation hearings, a copy of this directive shall be posted in the respective websites of the Commission (www.insurance.gov.ph) and National Life.

The Commission shall continue to release instructions from time to time in order to clarify or resolve other major issues submitted for consideration. Accordingly, all stakeholders are enjoined to regularly visit the said websites for major announcements.

SO ORDERED.

Manila, Philippines, 08 November 2013.

EMMANUEL F. DOOC
Insurance Commissioner

Copy furnished:

Hon. Cesar V. Purisima
Secretary
Department of Finance
DOF Bldg., BSP Complex,
Roxas Blvd., 1004 Metro Manila

National Life Insurance Company of the Philippines, Inc.
Thru Mr. Benjamin L. de Leon, President
NLIC Building, 6762 Ayala Avenue,
Makati City

Mr. Ermilando D. Napa,
Conservator
NLIC Building, 6762 Ayala Avenue,
Makati City

Policyholders Group
Thru Mrs. Katherine Yupangco
No. 13 Fonda St., Filinvest II,
Batasan Hills, Quezon City

Migriño Law Office
Atty. Joseph R. Migriño,
Counsel of the policyholders group,
Unit 706 City&Land Mega Plaza,
ADB Avenue cor. Garnet Road, Ortigas Center, Pasig City

Office of the Solicitor General
134 Amorsolo St., Legaspi Village,
Makati City