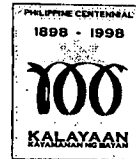




REPUBLIC OF THE PHILIPPINES
DEPARTMENT OF FINANCE
SECURITIES AND EXCHANGE COMMISSION
SEC Building, EDSA, Greenhills
City of Mandaluyong, Metro Manila



In the Matter of
G. COSMOS PHILIPPINES, INC.

CED Case No. 20-2488

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ORDER

G. COSMOS PHILIPPINES, INC. is a corporation registered with the Commission on August 8, 1999 under **S.E.C. Reg. No. 199911855** whose primary purpose stated in its articles of incorporation being as follows:

To create advertising campaign plans that will transmit in an effective manner as possible the message of the advertisers products and services through the utilization of print, television, radio cinema and other various advertising media and to render services in terms and/or merchandising, public relations and marketing counsel thereby offering a complete marketing service.

Upon receipt of the letter-complaints of Telford Roland Rizarri and Ruperto C. Garcia, an investigation was conducted to verify allegations stated therein. Pursuant thereto an Order dated May 28, 2001 was issued authorizing a team of one investigator and one examiner to look into all facts and circumstances of G. Cosmos to determine compliance with the provisions of the Securities and Regulation Code.

Based on documents gathered during the investigation and from said inspection, G. Cosmos Philippines, Inc. is found violating the provision of Section 8.1 of the Securities Regulation Code which particularly states, to wit:

Section 8.1. Securities shall not be sold or offered for sale or distribution within the Philippines, without a registration statement duly filed with and approved by the Commission. Prior to such sale, information on the securities, in such form and with such substance as the Commission may prescribe, shall be made available to each prospective purchaser (underscoring ours).

Section 3.1.b thereof enumerates by definition **Securities** which includes **Investment Contract**.

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SRC Rule 3.1.1 of the Implementing Rules and Regulations of R. A. 8799 defines **Investment Contract** as a contract, transaction or scheme (collectively "contract") whereby a person invests his money in a common enterprise and is led to expect profits from the efforts of others.

The definition of investment contract is adopted from the modified Howey Test originally defined by the US Federal Supreme Court in the case of SEC v. W. J. Howey Co., 328 US 293, 90 L Ed 1244, 66 S Ct 1100, 163 ALR 1043, rehden 329 US 819, 91 L Ed 697, 67 S Ct 27 as:

"a contract, transaction or scheme whereby a person invests money in a common enterprise expecting profits to accrue solely from the efforts of the promoter or third parties x x x"

Said definition was modified later in the US case SEC v. Glenn W. Turner, Enterprises, Inc. 474 F.2d 476 (9th Cir.1973), cert. Denied 414 U.S. 821, 94 S. Ct. 117, 38 L.Ed.2d 53. In the modified Howey test, the touchstone is the presence of an investment in a common venture premised on a reasonable expectation of profits to be derived from the entrepreneurial efforts of others. (69 Am Jur 2d S 36 p. 108) A mere token participation in an enterprise by the person investing capital does not prevent the contract from being classed as a security. Rather, in testing any transaction, form should be disregarded for substance and the emphasis should be on economic reality"(47 ALR 3d p. 1382 citing Bruner v. State (1970, Tex Crim 463 SW2d 205).

Investment contract has been viewed as a catch-all phrase designed to encompass novel devices which serve the same purpose as a security. Respondent's scheme of collecting from its members the advertising costs for its mail order sales in Japan falls within the purview of the definition of investment contract.

The elements of **Investment Contract** pursuant to the definition of the SRC Rules and Regulation are as follows:

- 1). A contract, transaction or scheme
- 2.) An investment of money
- 3). Investment is made in a common enterprise
- 4). Expectation of profits
- 5). Profits arise primarily from the efforts of others

A Contract, Transaction or Scheme (collectively "contract")

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The concept of investment contracts is a broad one, bringing many transactions having the nature of securities transactions, but not in the ordinary form, under the purview of the Securities Act x x x (69 Am Jur 2d 108 S36). It was given such a broad meaning as to include schemes for as long as it involves the use of the money of others on the promise of profits. Moreover, a writing is not essential for an investment contract. (1 Loss, Securities Regulation 2d Ed 489)

Under its G. System, G. Cosmos collects money for advertising from the average consumer for its mail order sales business. The money collected is used to conduct mail order sales in Japan through newspaper, television or magazine ads and profits are paid directly to the people who have paid the advertising costs. The individual who pays the advertising cost of a product receives his profit or income on the 5th-10th day or 20th-25th day of the month depending on the date of receipt of his Statement of Account which is received by him four (4) months from his first entry.

A person investing in G. Cosmos must execute a G. System Membership Agreement which embodies details of his investment in the company. Although respondent would label G. System otherwise, i.e., as an innovation in advertising and mail order sales, it still falls within the purview of the definition of investment contract.

As in the case of other security documents, form should be disregarded in favor of substance and emphasis should be placed on economic reality, and accordingly, labels affixed by the parties are of little moment, and statements in the instruments naming the relationship created thereby are not controlling. (79 CJS Supp. 170 S17).

Investment of Money

The modified Howey test for an investment contract requires, inter alia, the investment of money. It generally has been held that the investment of something other than money, such as services, is insufficient. x x x And it is clear that such investment must be made by the "investor", not by someone else for the "investors" benefit. (69 Am Jur 2d 109 S37). Under the G. System, a member desiring to earn profit or income has to make an entry or entries by paying the advertising costs of the products selected. Each entry for a featured window/product costs P1,650.00 for television, newspaper, magazine and newspaper flyers advertising. The amount of a member's investments in the company depends on the number of entries made plus the entry fee of P110.00 for each entry made.

Common Enterprise

Several tests or approaches have evolved to determine "common enterprise" and one of which is "narrow vertical" commonality approach (69 Am Jur 2d 113 S40) under which a common enterprise exists within the meaning of the Howey test where there is

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some interdependence or mutuality of interest in the success of the investor and the investment promoter (69 Am Jur 2d 115 S43). There is interdependence or mutuality of interest existing under the business concept of G. Cosmos. The success of a member's entries or investments depends largely on the entrepreneurial or marketing skills of the company. The latter earns a certain percentage of the profit of an investor as its own income. Without an entry by a member and the concomitant percentage in the profit, the company does not earn an income.

The common enterprise element is present in the case at hand as shown under the provision of SRC Rule 3.1-1(1)(a) of the Implementing Rules and Regulation of the Securities Regulation Code which clearly states that *when two or more investors "pool" their resources, there is a common enterprise, even if the promoter does not do more than receive a broker's commission.*

The members pool their resources when they make their entries for a certain product and these resources or funds are used by the company as capital in its business of mail order sales. From the thirty percent (30 %) profit generated from such sales, G. Cosmos receives five percent (5%) as its service charge or handling fee.

Expectation of Profits

As an element of an investment contract under the modified Howey test, the expected profits maybe derived from capital appreciation resulting from the development of the initial investment or from participation in earnings resulting from the use of the investors' funds (69 Am Jur 2d S38 p.110).

According to the G. System Agreement, the **rate of profit is 30%** of the total sales of the product. The percentage participation of a member in the 30% rate of profit has to be calculated on the basis of his proportionate share in the advertising cost of the product. As provided in the Agreement, a 5% service fee will be deducted from the member's receivable income. Such income is expected to be received by the member on the fourth month from date of his entry.

Profits Arise Primarily from the Efforts of Others:

The question under the modified Howey test is whether efforts made by those other than the investor are the undeniably significant ones, those essential managerial efforts which affect the failure or success of the enterprise (69 Am Jur 2d S 39 p.111) Under the G. System, a member's participation in the business of the respondent is the payment of the advertising costs of the product selected. On the other hand, upon admission of a member, G. Cosmos is responsible for the collection of money for advertising from other members for its mail order sales business, the advertising of the

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products selected by the members thru its associates in Japan, the conduct of the mail order sales, the tabulation of the sales, the preparation of the Statement of Accounts to be mailed to its members and the payment of the income after its service or handling fee has been deducted. Without these essential managerial efforts of the company, the individual who pays the advertising cost of a product will not receive his profit or income on the 5th-10th day or 20th-25th day of the month depending on the date of receipt of his Statement of Account which is received by him four (4) months from his first entry.

Since the securities offered for sale or distributed by the respondent corporation have not yet been registered with the Commission, there is an imperative need for said corporation to be enjoined from operating as such and from further engaging in the activities of selling, offering for sale or distributing securities in order to protect the interest of the investors and the public in general.

WHEREFORE, premises considered and in order to protect the investing public, G. COSMOS and its officers, directors, representatives and any and all persons claiming and acting for and in their behalf are hereby directed to CEASE AND DESIST from further engaging in activities of selling, offering for sale or distributing securities in order to protect the interest of the investors and the public in general.


SO ORDERED.

Mandaluyong City, Metro Manila, July 26, 2001.



LILIA R. BAUTISTA

Chairperson



FE ELOISA C. GLORIA

Commissioner

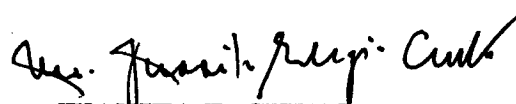


EDIJER A. MARTINEZ

Commissioner

JOSELIA J. POBLADOR

Commissioner



JUANITA E. CUETO

Commissioner