Republic of the Philippines
Department of Trade Industry
Securities and Exchange Commission
SEC Bldg. EDSA, Greenhills, Mandaluyong City

COMMISSION *EN BANC*

In the Matter of the Petition for the Revocation of the Certificate of Registration of **Linearworks Realty Development Corporation,**

SEC En Banc Case No. 07-10-205

(EPD Reference No. 2010-177-CID)

Seven Oaks Properties, Inc.,
Petitioner.

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DECISION

This refers to the Appeal to the Commission *En Banc,* filed by petitioner Seven Oaks Properties, Inc., from the Enforcement and Prosecution Department's ("EPD," for brevity) 24 June 2010 Order that dismissed the Petition for the Revocation of the Certificate of Registration of Linearworks Realty Development Corporation.

Linearworks Realty Development Corporation is registered with the Commission under Company Registration No. CS200712611 since 21 August 2007. Its primary purpose is: "To own, use, improve, develop, subdivide, sell, exchange, lease, and hold for investment or otherwise, real estate of all kinds, including buildings, houses, apartments and other structures."[1]

Its authorized capital stock is eighteen million pesos (Php 18,000,000.00), divided into 5,000 Class A shares with par value at ten pesos (Php 10.00) each, and 1,795 Class B shares with par value of ten thousand pesos (Php 10,000.00) each.[2] Its shares are subscribed as follows:[3]

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[1] Articles of Incorporation, Article II;
[2] Articles of Incorporation, Article VII;
[3] Articles of Incorporation, Article VIII;

Shareholder	Nationality	Class of Share	Par Value	Number of Shares Subscribed	Amount Subscribed (subscribed shares x par value)
Agnes A. Lomarda	Filipino	A	Php 10.00	2,000	Php 20,000.00
Daniel Lomarda	Filipino	A	Php 10.00	2,000	Php 20,000.00
Johnathan Gonzales	Filipino	A	Php 10.00	1,000	Php 10,000.00
Sugaya Shozo	Japanese	B	Php 10,000.00	1	Php 10,000.00
Noboru Soma	Japanese	B	Php 10,000.00	1	Php 10,000.00
Linearworks Corporation	Japanese	B	Php 10,000.00	1,793	Php 17,930,000.00
Total				6,795	Php 18,000,000.00

Seven Oaks Properties, Inc. filed a Petition for the Revocation of the Certificate of Registration of Linearworks Realty Development Corporation on 16 February 2010 with the EPD. The petitioner alleged that Linearworks Realty Development Corporation's equity structure was designed to circumvent the constitutional and statutory limitations on foreign ownership of private lands in our country.

Article XII, Section 7 of the 1987 Constitution, in relation to Sections 22 and 23 of Commonwealth Act No. 141, provides that, in order for a corporation to own land, at least sixty *per centum* (60%) of its capital stock must belong wholly to Philippine citizens. Conversely, the participation of foreign nationals in a corporation owning land is limited to a maximum of up to forty *per centum* (40%) of the equity only.

In furtherance of such constitutional and statutory restrictions on foreign ownership, Section 2 of Commonwealth Act No. 108[4] punishes any simulation of the ownership of the capital stock by Philippine citizens that are made for the purpose of evading the said restrictions. And, Section 3 of the same Act mandates that any corporation that commits such a violation must be dissolved.

[4] As amended by Republic Act 421, Republic Act 134, Republic Act 6084, and Presidential Decree 715.

Since Linearworks Realty Development Corporation is engaged in real estate activities, including the ownership of land, the said restrictions necessarily apply to it. And thus, at least sixty *per centum* (60%) of its capital stock must belong wholly to Philippine citizens, and foreign ownership is permitted only up to forty *per centum* (40%) of the total equity.

Petitioner argued that the *per centum* of participation by foreign nationals in Linearworks Realty Development Corporation exceeds the restrictions, and actually amounts to 99.72% of the total equity since the total amount subscribed by the Japanese nationals is Php 17,950,000.00 out of the total Php 18,000,000.00 authorized capital stock.

However, the EPD rejected the petitioner's arguments. The EPD maintained that the basis for determining the level of foreign participation is the number of shares subscribed, regardless of the par value. Applying such an interpretation, the EPD ruled that the foreign equity participation in Linearworks Realty Development Corporation amounts to 26.41% of the corporation's capital stock since the amount of shares subscribed by foreign nationals is 1,795 only out of the 6,795 total shares. Thus, the subject corporation is compliant with the 40% limit on foreign equity participation. Accordingly, the EPD dismissed the complaint, and did not pursue any investigation against the subject corporation.

Unsatisfied with the EPD's stance, the petitioner filed the present appeal to on 13 July 2010.

The main legal issue submitted by the petitioner for resolution is whether the determination of foreign equity participation ought to be based on the number of shares only, or whether it should be based on the actual equity investment or amount subscribed, i.e., number of shares multiplied by the par value. In other words, the issue is whether or not the par value of shares should be considered in determining the level of foreign equity participation in a corporation.

In order to resolve this issue, we look at the intent and purpose of the constitutional and statutory limitations on foreign equity of corporations owning land.

In this regard, the DOJ's Opinion No. 130, series of 1985, is instructive. Then Minister of Justice Estelito P. Mendoza, addressing the Board of Investments, discussed, in part, that:

> "The constitutional ban on the acquisition of public and private land by aliens or by corporations with less than 60% Philippine equity is a provision carried over from the 1935 Constitution that is intended to ensure, among other purposes, the conservation for Filipino posterity of land and indigenous natural resources, which constitute the exclusive heritage of the Filipino nation (Vol. X, Constitutional Convention Records Journal Nos. 131-

> 139, pp. 144 et seq., Sinco, Political Law, 1962 Ed. p. 445). This Ministry has had occasion to state in several opinions, that it is implicit in this provision, **even if it refers merely to ownership of stock in the corporation holding the land or natural resource concession, that the nationality requirement is not satisfied unless it satisfies the criterion of beneficial ownership, i.e., Filipinos are the principal beneficiaries in the exploitation of natural resources** (Op. No. 144, s. 1977; Roman Catholic Apostolic Adm. of Davao, Inc., vs. Land. Reg. Com. 102 Phil. 596[1957]) **and that in applying the same "the primordial consideration is situs of control, whether in a stock or non-stock corporation"** (Op. No. 178, s. 1974). The framers of the constitution, in limiting the disposition, exploration, development, exploitation or utilization of the natural resources of Philippines to citizens or to corporations or associations at least 60% of the capital of which is owned by such citizens, could not have intended "any interest less than **full and absolute ownership by Philippine citizens of the 60% capital**", and any other interpretation would do violence to the policy and intent behind these and related constitutional provisions of insuring the conservation of the natural resources of the Philippines for its citizens (Op. No. 171, s. 1974). As stated in Register of Deeds vs. Ung Sui Si Temple (97 Phil. 58), the purpose of the sixty per centum requirement is obviously to ensure that corporations and associations allowed to acquire agricultural land or to exploit natural resources '**shall be controlled by Filipinos**'."

In short, the constitutional and statutory restrictions were enacted in order to conserve lands and other natural resources for the benefit and control of Philippine citizens.

In fact, in line with the said purpose, the Foreign Investments Act of 1991[5] and its implementing rules and regulations provide the basis for determining whether a corporation may be treated as a Philippine national in accordance with the constitutional and statutory restrictions on foreign equity. Section 1 of the Implementing Rules and Regulations of the Foreign Investments Act of 1991, provides that:

> "b. Philippine national shall mean a citizen of the Philippines or a domestic partnership or association wholly owned by the citizens of the Philippines; or a corporation organized under the laws of the Philippines of which at least sixty percent (60%) of the **capital stock outstanding and entitled to vote is owned and held by citizens of the Philippines;** or a corporation organized abroad and registered as doing business in the Philippines under the Corporation Code of which 100% of the capital stock outstanding and entitled to vote is wholly owned by Filipinos or a trustee of funds for pension or other employee retirement or separation benefits, where the trustee is a Philippine national and at least sixty percent (60%) of the fund **will accrue to the benefits of the Philippine nationals;** Provided, that where a corporation and its non-Filipino stockholders

[5] Republic Act 7042, as amended.

> own stocks in Securities and Exchange Commission (SEC) registered enterprise, at least sixty percent (60%) of the capital stock outstanding and entitled to vote of each of both corporations must be owned and held by citizens of the Philippines and at least sixty percent (60%) of the members of the Board of Directors of each of both corporations must be citizens of the Philippines, in order that the corporation shall be considered a Philippine national. The control test shall be applied for this purpose.
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> Compliance with the required Filipino ownership of a corporation shall be determined on the basis of outstanding capital stock whether fully paid or not, but only such stocks which are generally entitled to vote are considered.
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> **For stocks to be deemed owned and held by Philippine citizens or Philippine nationals, mere legal title is not enough to meet the required Filipino equity. Full beneficial ownership of the stocks, coupled with appropriate voting rights is essential.** Thus, stocks, the voting rights of which have been assigned or transferred to aliens cannot be considered held by Philippine citizens or Philippine nationals.
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> Individuals or juridical entities not meeting the aforementioned qualifications are considered as non-Philippine nationals."

With these considerations in mind, it is clear that, the important criteria for determining compliance with the foreign equity restrictions are: (1) control and (2) beneficial ownership. We must ensure that a corporation, engaged in activities reserved to Philippine citizens, is: first, under the effective control of Philippine citizens; and second, the Philippine citizens are the main beneficiaries of the business activity.

And, in order to determine the state of such criteria, we need to look into the total number of shares subscribed by Philippine citizens out of the total outstanding capital stock, and crucially, the rights, privileges or restrictions conferred upon such shares.

Now, a share's par value is "simply an amount fixed as the nominal value of the interest so specified, which amount likewise indicates the sum of money or value of property or services which a subscriber is represented as having contributed to the corporation in exchange for such share in its ownership."[6] The par value of the share does not determine the rights, privileges or restrictions of the share. This means that the par value of the subscribed shares is actually irrelevant in determining compliance with the constitutional and statutory restrictions on foreign equity.

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[6] 13 American Jurisprudence § 176.

What we need to look at is the corporation's articles of incorporation since except as otherwise provided in the articles of incorporation and stated in the certificate of stock, each share shall be equal in all respects to every other share.[7] In other words, the articles of incorporation provide the rights, privileges or restrictions conferred upon the shares. Any other document, or agreements purporting to classify shares, and conferring respective rights, privileges or restrictions upon each type of shares is ineffective with respect to the corporation.

In the present case, an examination of Linearworks Realty Development Corporation's articles of incorporation reveal that while the shares may be classified to two types having different par value, there is no provision conferring different rights, privileges or restrictions on each type. Thus, the shares, although they have different par values, are equal in every rights, privileges or restrictions. In particular, every share, regardless of par value, is entitled to the same voting rights, the exact same value of dividends, and at the time of liquidation, each share is entitled to same rights and interests over the remaining assets for distribution – which may include land.

Considering that all the shares in the subject corporation have equal rights, control, and economic rights over the corporation and its assets is solely dependent upon the number of shares subscribed, irrespective of par value. It is now simply a matter of determining the number of shares subscribed by Philippine citizens out of the total outstanding capital stock in order to determine compliance with the forty percent (40%) foreign equity restriction.

Thus, in this respect we find no error in the assailed order made by the EPD. The EPD did not err when it did not take into account the par value of shares in determining compliance with the constitutional and statutory restrictions on foreign equity.

However, we are aware that some unscrupulous individuals employ certain schemes to circumvent the constitutional and statutory restrictions on foreign equity. In the present case, the fact that the shares of the Japanese nationals have a greater par value but only have similar rights to those held by Philippine citizens having much lower par value, is highly suspicious. This is because a reasonable investor would expect to have greater control and economic rights than other investors who invested less capital than him. Thus, it is reasonable to suspect that there may be secret arrangements between the corporation and the stockholders wherein the Japanese nationals who subscribe to the shares with greater par value actually have greater control and economic rights contrary to the equality of shares based on the articles of incorporation.

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[7] Corporation Code, Section 6.

With this in mind, we find it proper for the EPD to investigate the subject corporation. The EPD is advised to avail of the Commission's subpoena powers in order to gather sufficient evidence, and file the necessary complaint.

Incidentally, a perusal of the subject corporation's 2010 General Information Sheet on file with the Commission's records, reveals that Noboru Soma, a Japanese national, is the corporate treasurer.

We note that that pursuant to the provisions of the Anti-Dummy Law, aliens are banned from being elected or appointed to management positions as president, vice-president, treasurer, auditor, etc. in firms engaged in wholly or partially nationalized business, although they can be elected directors in proportion to their allowable participation or share in the capital of such companies.[8]

WHEREFORE, premises considered, the Appeal is hereby **DISMISSED** for lack of merit. The Enforcement Prosecution Department (EPD) is hereby **ORDERED** to investigate the subject corporation, its officers and stockholders for possible violations, and to recommend the imposition of administrative sanctions if warranted under the circumstances.

Further, the EPD is hereby **DIRECTED** to report the subject corporation and Noboru Soma to the Department of Justice, the Bureau of Immigration, and other related agencies for violation of the Anti-Dummy Law.

SO ORDERED.

Mandaluyong City, 25 November 2010.

...E B. BARIN
Chairperson

MA. JUANITA E. CUETO
Commissioner

RAUL J. PALABRICA
Commissioner

[8] Commonwealth Act No. 108, Section 2-A, as amended by P.D. 715.

MANUEL HUBERTO B. GAITE
Commissioner

ELADIO M. JALA
Commissioner