Republic of the Philippines
Department of Finance
SECURITIES AND EXCHANGE COMMISSION
SEC Building, EDSA, Greenhills
Mandaluyong City Metro Manila
Philippines

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Angara Abello Concepcion
Regala & Cruz Law Offices
ACCRA Building
122 Gamboa St., Legaspi Village
0770 Makati City

SEC Opinion No. 06-36
Corporate Nationality under the FIA; Reclassification of Shares of Stock; Required Equity under the Financing Company Act

Attention: ***Atty. Tadeo F. Hilado***

Gentlemen:

This refers to your letter dated 28 April 2006 whereby you posited the following inquiries, namely:

(1) Whether or not the proposed reclassification of the shares of stocks of your client, BOT Lease Holdings Philippines (BOT Holding), and the transfer of some of the reclassified shares from an existing stockholder to another will not affect BOT Holding's status as a Philippine national as defined in the Foreign Investments Act (FIA); and

(2) Whether or not, with the resulting ownership of the capital stock of BOT Holding, it will still maintain its status as a Philippine national whose investment in the shares of stock of BOT Lease Finance Philippines, Inc. (BOT Finance) will be considered Filipino-owned.

The "Foreign Investments Act" defines a "Philippines national" as thus:

> The term "Philippine national" shall mean a citizen of the Philippines; of a domestic partnership or association wholly owned by 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 one hundred percent (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 benefit of Philippine nationals: Provided, That where a corporation and its non-Filipino stockholders own stocks in a 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."[1] [Emphasis supplied]

Applying the foregoing definition, a corporation with sixty percent (60%) Filipino and forty percent (40%) foreign equity ownership is considered a Philippine national, for purposes of investment.[2] For as long as the percentage of Filipino equity over the capital stock of all the corporate stockholders is at least sixty percent (60%) thereof, the *entire stockholdings* of the corporation shall be considered as of Philippine nationality.[3] Conversely, once the foreign equity percentage participation increases beyond (40%), the corporation shall no longer be a Philippine national under the control test, but a foreign corporation covered by the Foreign Investments Act (FIA).[4]

The computation of the sixty percent (60%) Filipino ownership for purposes of determining whether or not a corporation is a Philippine national is based on the *total number of outstanding capital stock entitled to vote*—irrespective of amount of the par value of the shares,[5] and likewise regardless of whether or not such shares have been fully or partially paid.[6]

Based on the present distribution of the shareholdings of BOT Holding it is no doubt of Philippine nationality, it being evident in *Table A* and *Chart A*, herein annexed, that the equity participation of Filipinos and foreigners over the outstanding capital stock of the corporation is sixty percent (60%) and forty percent (40%) respectively.

Even after BOT Holding reclassifies its shares into "Class A" and "Class B," the having the par values of Two Hundred Pesos (Php200.00) and Twenty-Five Thousand Pesos per share, respectively, as shown in the annexed *Table B*, BOT Holdings will still maintain its status as a Philippines national since the resulting equity percentage participation over the outstanding capital stock would still comply with the requirements of the FIA. In fact, upon reclassification of its

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[1] Sec. 3(a), Foreign Investments Act (RA 7042, as amended by Republic Act No. 8179)
[2] SEC Opinion addressed to Ms. Andrea Laban, 02 June 2003
[3] SEC Opinion addressed to Commissioner Armi Jane R. Borje, 02 June 2003
[4] SEC Opinion addressed to Mr. Job M. Mayo, Jr., 10 August 2004
[5] SEC Opinion addressed to Atty. Tadeo F. Hilado, 06 July 2005
[6] Section 137, Corporation Code of the Philippines

shares, the Filipino equity percentage would increase to 83.81%, while foreign equity will be reduced to only 16.19%, as shown in the annexed *Table* C.

The classification of shares by a corporation, or in this case, its reclassification, is allowed by the Corporation Code. Section 6 of the Code provides:

> "Sec. 6. The shares of stock of stock corporations may be divided into classes or series of shares, or both, any of which classes or series of shares may have such rights, privileges or restrictions as may be stated in the articles of incorporation: Provided, That no share may be deprived of voting rights except those classified and issued as 'preferred' or 'redeemable' shares, unless otherwise provided in this Code: Provided, further, That there shall always be a class or series of shares which have complete voting rights. Any or all of the shares or series of shares may have a par value or have no par value as may be provided for in the articles of incorporation.
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> "A corporation may, furthermore, classify its shares for the purpose of insuring compliance with constitutional or legal requirements."[7]

A corporation may, on its own discretion, for reasons of expediency, for monitoring purposes, or to insure compliance with constitutional or legal requirements, provide for classification of shares. Each class of shares may be assigned varying par values, and likewise, one class of shares may be more than the others.[8]

> "There is neither a constitutional nor a statutory mandate for the classification of corporate shares into class "A" and class "B" shares. Such arrangement is only a device internally adopted by Philippine companies to facilitate monitoring of foreign equity in the company. This practice is recognized, but not mandated, by the Corporation Code which allows a corporation to classify its shares for the purpose of insuring compliance with constitutional or legal requirements.[9]"

It is however understood that the classification of shares should be based on substantial distinctions.[10]

This Commission likewise affirms that the subsequent sale by Filipino stockholders of all of its 893 "Class B" shares to the foreigners will not affect the status of BOT Holding as a Philippine national. After the transfer, it is evident, as can be gleaned from the annexed *Table D*, that the resulting equity percentage

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[7] Section 6, Corporation Code of the Philippines

[8] De Leon, Hector S. The Corporation Code of the Philippines Annotated, 2002 Edition, p. 66

[9] *Ibid*; DOJ Opinion No. 195, October 3, 1989

[10] Where no difference in "rights, privileges or restrictions" is provided for as required by Section 6, as where "the only difference between the series is that only B-1 Series shall be initially offered to the public and sold through the exchanges while B-2 Series shall be similarly offered and sold at a later date as the board of directors may determine," the classification should not be allowed. (*Supra, p. 65*; citing SEC Opinion, 15 March 1989)

participation of the Filipino and foreign stockholders of the corporation over the outstanding capital stock will be sixty percent (60%) and forty percent (40%), still in compliance with the requirements of the FIA.

In respect to the second matter that you raised, that is, whether or not, with the resulting ownership of the capital stock of BOT Holding, it will still maintain its status as a Philippine national whose investment in the shares of stock of BOT Finance will be considered Filipino-owned—we answer in the affirmative.

BOT Finance, a leasing and financing company, is a corporation covered by RA 5980, as amended, otherwise known as the Financing Company Act (FCA), which mandates that at least forty percent (40%) of the voting stock of financing companies should be owned by citizens of the Philippines.

> "SEC. 6. Form of organization and capital requirements. — Financing companies shall be organized in the form of stock corporations *at least forty percent (40%) of the voting stock of which is owned by citizens of the Philippines* and shall have a paid-up capital of not less than Ten million pesos (P10,000,000) in case the financing company is located in Metro Manila and other first class cities, Five million pesos (P5,000,000) in other classes of cities and Two million five hundred thousand pesos (P2,500,000) in municipalities: Provided, however, That no foreign national may be allowed to own stock in any financing company unless the country of which he is a national accords the same reciprocal rights to Filipinos in the ownership of financing companies or their counterpart entities in such country: and Provided, further, That financing companies duly existing and in operation before the effectivity of this Act shall comply with the minimum capital requirement within one (1) year from the date of the said effectivity."[11] [Emphasis supplied]

BOT Holding, which presently owns forty percent (40%) equity percentage participation over the *voting stock* of BOT Leasing, as can be gleaned from the annexed *Table E* and *Chart B*, will remain to be a Philippine national under the purview of the FIA even after the proposed reclassification and subsequent transfer of shares, for reasons discussed earlier. Since BOT Holding will continue to have the status of a Philippine national, its forty percent (40%) interest in the voting stock of BOT leasing are deemed Filipino-owned; and as such, the former continue to hold such interest in latter, and is, by all means compliant with the nationality requirements provided for by the FCA.

Parenthetically, with respect to the nationality of BOT Leasing, sinceHidden text while BOT Holding is a Philippine national, the status of BOT Leasing is and, after the reclassification of shares of the former, will continue to be that of a Foreign national. Since the FCA does not provide a "control test," that is, a provision for determining the nationality of a corporation, the question of whether not a corporation is a of Philippine nationality for the purpose of

[11] Section 6, Financing Company Act (RA 5980, as amended)

complying with the prescribed equity percentage participation under the act, and whether or not financing company is itself of Philippine nationality, shall have to be determined by the provisions of the FIA—the general law governing foreign investments.

The FIA, as discussed earlier, considers a corporation a Philippine national if it is one that has been organized under the laws of the Philippines, and at least sixty percent (60%) of its capital stock outstanding and entitled to vote is owned and held by citizens of the Philippines.[12] With respect to BOT Leasing, it is a not a Philippine national, but a Foreign national because the total equity percentage participation over the capital stock outstanding and entitled to vote held by a Philippine national (BOT Holding) amounts to only forty percent (40%), as shown in *Table E* and *Chart B*.

Thus, BOT Holding is a Philippine national as defined under the FIA, and complies with the requirement of the FCA, that is, it own and will continue to own forty percent (40%) of the voting stock of BOT Leasing. BOT Leasing on the other hand is a Foreign national, and will continue to remain as such even after the proposed reclassification of shares by BOT Holding since the total subscribed equity percentage participation of Philippine nationals has not reached the sixty percentum (60%) required by the FIA.

It shall be understood that the opinion rendered is based solely on facts and circumstances disclosed in the queries and relevant solely to the particular issues raised therein and shall not be used in the nature of a standing rule binding upon the Commission in other cases whether of similar or dissimilar circumstances.

For your information and guidance.

Very truly yours,

VERNETTE G. UMALI- PACO
General Counsel

[12] Sec. 3(a), Foreign Investments Act (RA 7042, as amended by Republic Act No. 8179)