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

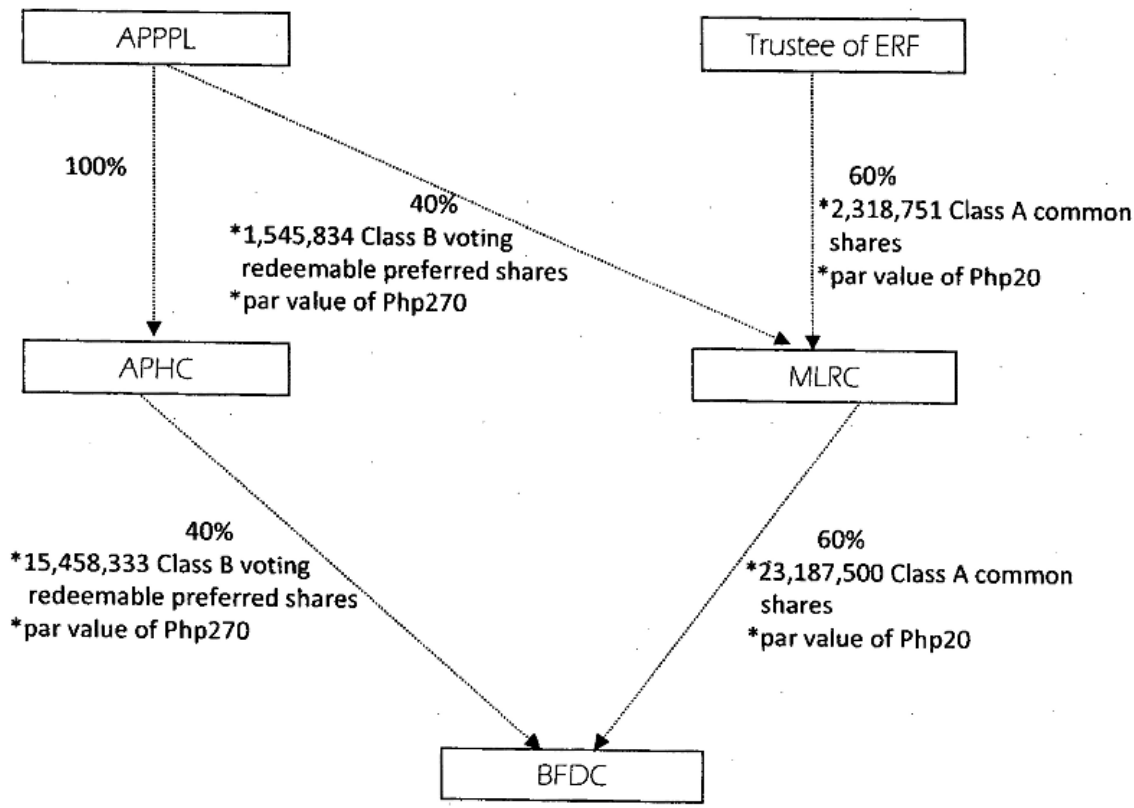
18 August 2010
SEC-OGC Opinion No. 10-23
Re: Ownership Structure of a Land-Owning Corporation

CASTILLO LAMAN TAN PANTALEON & SAN JOSE
The Valero Tower, 122 Valero St.,
Salcedo Village, Makati City

Attention: Attys. Teodulo G. San Juan, Jr. and Erdelyne C. Go

Sir/Madam:

This refers to your 15 January 2010 letter requesting confirmation of your position that the following proposed ownership structure of BFDC does not violate the nationality restrictions imposed by the Constitution and applicable statutes upon land-owning corporations:



You mentioned that:

APPPL is an entity organized under the laws of Singapore and is wholly-owned by Singaporean nationals. It owns 100% of **APHC**, a corporation organized and existing under Philippine laws. It will joint venture with the trustee (hereinafter, "the **Trustee**") of an Employee Retirement Fund ("**ERF**") to form **MLRC**, another corporation organized and existing under Philippine laws.

For purposes of this request, you want us to assume that the Trustee is itself a Philippine National within the context of Republic Act ("RA") No. 7042, or the Foreign Investments Act ("FIA") of 1991, as amended, and that at least 60% of the ERF will accrue to the benefit of Philippine Nationals.

The Trustee, acting for the beneficial interest of the ERF, shall own and hold 2,318,751 MLRC Class A common shares with par value of Php20.00 per share, comprising 60% of the total outstanding and voting capital stock of MLRC. On the other hand, APPPL shall own and hold 1,545,834 MLRC Class B voting redeemable preferred shares with par value of Php270.00 per share, making up 40% of the total outstanding and voting capital stock of MLRC.

APHC and MLRC will acquire shares of stock in **BFDC**, a corporation which will own land(s) in the Philippines. MLRC shall own and hold 23,187,500 BFDC Class A common shares with par value of Php20.00 per share, comprising 60% of the total outstanding and voting capital stock of BFDC. Meanwhile, APHC shall own and hold 15,458,333 Class B BFDC voting redeemable preferred shares with par value of Php270.00 per share, making up 40% of the total outstanding and voting capital stock of BFDC.

You further request us to assume that at least 60% of the directors of both MLRC and BFDC shall be Filipino citizens.

The legal capacity of a corporation to acquire land(s) in the Philippines is regulated by the Constitution and applicable statutes.

Section 7, Article XII of the 1987 Constitution provides that *"[s]ave in cases of hereditary succession, no private lands shall be transferred except to individuals, corporations or associations qualified to acquire or hold lands of public domain."* Those qualified are "... *Filipino citizens, or corporations or associations at least sixty per centum of whose capital is owned by such citizens.*"[1]

[1]CONST. (1987), Art. XII, Sec. 2.

As to statutory provisions, Sections 22 and 23 of Commonwealth Act No. 141, otherwise known as the Public Land Act, provide:

> "Section 22. Any citizen of lawful age of the Philippines, and any such citizen not of lawful age who is a head of the family, and *any corporation or association of which at least sixty per centum of the CAPITAL STOCK xxx belongs wholly to citizens of the Philippines*, and which is organized and constituted under the laws of the Philippines, xxx authorized under their charter, to do so, may purchase any tract of public agricultural land disposable under this Act...." (Emphasis supplied)

> "Section 23. No person, corporation, association or partnership *other than those mentioned in the last preceding section*, may acquire or own agricultural public land *or land of any other denomination or classification*, which is at the time or was originally, really or presumptively of the public domain, or any permanent improvement thereon, or any real right on such land and improvement ...." (Emphasis provided)

In relation thereto, Section 3(a) of the FIA provides:

> "(a) the term *Philippine national* shall mean a citizen of the Philippines; or 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; xxx; 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 as Philippine national." (Emphasis supplied).

Paragraph 7 of the 1967 SEC Rules ("SEC Rules") – which were promulgated on 28 February 1967[2] to implement the requirements of the Constitution and the pertinent laws that the controlling interests in enterprises engaged in the exploitation of natural resources shall be owned by Filipino citizens – provides:

> "Shares belonging to corporations or partnerships at least 60% of the capital of which is owned by Filipino citizens shall be considered as of Philippine nationality, but if the percentage of Filipino ownership in the corporation or partnership is less than 60%, only the number of shares corresponding to such percentage shall be counted as of Philippine nationality. Thus, if 100,000 shares are registered in the name of a

[2]Substantially reiterated on 7 September 1972 and approved by the then Secretary of Commerce and Industry on 12 September 1972, as cited in DOJ Opinion No. 018, Series of 1989.

corporation or partnership at least 60% of the capital stock or capital, respectively, of which belong to Filipino citizens, all of the said shares shall be recorded as owned by Filipinos. But if less than 60%, or say, only 50% of the capital stock or capital of the corporation or partnership, respectively, belongs to Filipino citizens, only 50,000 shares shall be counted as owned by Filipinos and the other 50,000 shares shall be recorded as belonging to aliens."

Under the above-quoted SEC Rules, there are two cases in determining the nationality of the Investee Corporation. The first case is the 'liberal rule', later coined by the Commission as the **Control Test** in its 30 May 1990 Opinion, and pertains to the portion in said Paragraph 7 of the 1967 SEC Rules which states, *'(s)hares belonging to corporations or partnerships at least 60% of the capital of which is owned by Filipino citizens shall be considered as of Philippine nationality.'* Under the liberal Control Test, **there is no need to further trace the ownership of the 60% (or more) Filipino stockholdings of the Investing Corporation since a corporation which is at least 60% Filipino-owned is considered as Filipino.**[3]

The second case is the Strict Rule or the **Grandfather Rule Proper** and pertains to the portion in said Paragraph 7 of the 1967 SEC Rules which states, "*but if the percentage of Filipino ownership in the corporation or partnership is less than 60%, only the number of shares corresponding to such percentage shall be counted as of Philippine nationality.*" Under the Strict Rule or Grandfather Rule Proper, **the combined totals in the Investing Corporation and the Investee Corporation must be traced (i.e., "grandfathered")** to determine the total percentage of Filipino ownership.[4]

In other words, the **Grandfather Rule** or the second part of the SEC Rule **applies only** when the 60-40 Filipino-foreign equity ownership is in doubt (i.e. **in cases where the joint venture corporation with Filipino and foreign stockholders with less than 60% Filipino stockholdings [or 59%] invests in other joint venture corporation which is either 60-40% Filipino-alien or 59% less Filipino**). **Stated differently, where the 60-40 Filipino-foreign equity ownership is not in doubt, the Grandfather Rule will not apply.**[5]

In two (2) of its most recent opinions on the qualification of corporations to own lands[6], the Commission applied the Control Test and dispensed with further inquiry into the ownership of the shareholders in both investing and investee corporations. This is because it was clearly established that the participating corporations are 60% owned by Filipino citizens.

Applying the foregoing, particularly the Control Test, MLRC is deemed as a Philippine national because: (1) sixty percent (60%) of its outstanding capital stock

[3]DOJ Opinion No. 020, Series of 2005.
[4]Ibid.
[5]Ibid.
[6]SEC-OGC Opinion No. 07-22 dated 7 December 2007; and SEC-OGC Opinion No. 03-08 dated 15 January 2008.

entitled to vote is owned by a Philippine national, the Trustee; and (2) at least sixty percent (60%) of the ERF will accrue to the benefit of Philippine nationals.

Still pursuant to the Control Test, MLRC's investment in 60% of BFDC's outstanding capital stock entitled to vote shall be deemed as of Philippine nationality, thereby qualifying BFDC to own private land.

Further, under, and for purposes of, the FIA, MLRC and BFDC are both Philippine nationals, considering that: (1) sixty percent (60%) of their respective outstanding capital stock entitled to vote is owned by a Philippine national (i.e., by the Trustee, in the case of MLRC; and by MLRC, in the case of BFDC); and (2) at least 60% of their respective board of directors are Filipino citizens.

That MLRC and BFDC shares are classified into (1) common shares -- which are generally entitled to vote -- and (2) redeemable preferred voting shares, with different par values, is of no moment. It is now settled that the test for compliance with the nationality requirement is based on the total outstanding capital stock irrespective of the amount of the par value of the shares.[7]

Thus, we confirm your position.

This opinion is based solely on the facts disclosed in the query and relevant solely to the particular issues raised therein. It shall likewise be understood that the foregoing shall not be used in the nature of a standing rule binding upon the Commission in other cases or upon the courts.[8] If, upon investigation, it will be disclosed that the facts relied upon are different, this Opinion shall be rendered void.

Please be guided accordingly.

Very truly yours,

VERNETTE G. UMALI-PACO
General Counsel

[7]SEC Opinion No. 49-04 dated 22 December 2004; SEC Opinion No. 30-06 dated 21 September 2006; SEC-OGC Opinion No. 07-22 dated 7 December 2007; and SEC-OGC Opinion No. 03-08 dated 15 January 2008.

[8]Paragraph 7, SEC Memorandum Circular No. 15, Series of 2003.