Republic of the Philippines
Department of Finance
Securities and Exchange Commission

OFFICE OF THE GENERAL COUNSEL

21 November 2018

SEC-OGC Opinion No. 18-20
RE: Application of the Control Test to Retail Companies pursuant to the Retail Trade Liberalizaton Act.

ATTY. JOFRED PAUL P. JANDAYAN
No. 7 The Coating Industries Compound
Sheridan St., Shaw Boulevard
Mandaluyong City

Dear Atty. Jandayan:

This refers to your letter dated 25 October 2016 requesting for an opinion on whether your client (Company A), which is a 60% Filipino and 40% foreign-owned corporation, can invest in a domestic corporation (Company B) which will be incorporated together with other Filipino individuals to engage in the restaurant business, an activity considered as retail and therefore subject to 100% Filipino ownership.

You mentioned that Company B is required by law to be 100% Filipino-owned. You also posited that by applying the Control Test, as long as Company A is 60% owned by Filipinos, its existing and would-be shareholdings in Company B shall be considered owned by Filipinos for purposes of computing the required Filipino equity for Company B. You quoted the decision of the Supreme Court in *Narra Nickel Mining and Development Corporation, et al. v. Redmont Consolidated Mines Corporation*[1] wherein the High Court acknowledged the existence of two tests, the Control Test and the Grandfather Rule, as a means to determine the nationality of a corporation engaged in nationalized activities. You also referred to paragraph 7 of DOJ Opinion No. 020, Series of 2005, wherein the Department of Justice described the Control Test as a "liberal rule" in determining the nationality of a corporation.

[1] G.R. No. 195580, 21 April 2014

We answer in the negative. **Section 5** of the Retail Trade Liberalization Act (RTLA)[2] provides for the extent of allowable foreign investment in retail trade business:

> Section 5. Foreign Equity Participation. - Foreign-owned partnerships, associations and corporation formed and organized under the laws of the Philippines may, upon registration with the Securities and Exchange Commission (SEC) and the Department of Trade and Industry (DTI), or in case of foreign owned single proprietorships, with the DTI, engage or invest in the retail trade business, subject to the following categories.
>
> **Category A – Enterprises with paid-up capital of the equivalent in Philippine Peso of less than Two million five hundred thousand US dollars (US$2,500,000.00) shall be reserved exclusively for Filipino citizens and corporations wholly owned by Filipino citizens.**
>
> **xxxx**

Furthermore, **Section 1, Rule III** of the Rules and Regulations Implementing Republic Act No. 8762 provides that:

> Section 1. Foreign Equity Participation – Partnerships, associations and corporations, partially or wholly-owned by foreigners, formed and organized under the laws of the Philippines may upon registration with the Securities and Exchange Commission (SEC), or in case of foreign-owned single proprietorships, with the Department of Trade and Industry (DTI), may engage or invest in the retail trade business, subject to the following categories:
>
> **Category A – Enterprises with paid-up capital of the equivalent in Philippine Pesos of less than Two million five hundred thousand US dollars (US$2,500,000.00) shall be reserved exclusively for Filipino citizens and corporations wholly owned by Filipino citizens.**
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> **xxxx**

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[2] An Act Liberalizing the Retail Trade Business, Repealing for the Purpose Republic Act No. 1180, As Amended, and for Other Purposes [Retail Trade Liberalization Act 2000], Republic Act 8762, Section 5 (2000)

It is clearly provided that all investments in retail trade enterprises shall be **reserved exclusively** to **corporations <u>wholly-owned by Filipino citizens when their paid-up capital is less than the peso equivalent of US$ 2,500,000.00</u>**. This rule is likewise reflected in the 11th Foreign Investment Negative List.[3]

When stating that Company B is required by law to be 100% Filipino-owned, this presupposes that Company B has a paid-up capital of less than US$2,500,000.00 or its peso equivalent. Otherwise, if Company B satisfies the capitalization requirement, it would no longer be required to be 100% Filipino-owned per the afore-quoted provision.

Assuming that Company B is required to be 100% Filipino-owned for having a capitalization less than US $ 2,500,000.00, your position that the Control Test should be used, and that Company B should be considered Filipino as long as Company A is 60% Filipino-owned, is misplaced. It has long been held that the Control Test merely creates the legal fiction that when a corporation is at least 60% Filipino owned, it is considered or presumed to be Filipino. However, the principle should not apply to corporations that are subject to the strictest nationality requirement (i.e. those required to be 100% Filipino-owned). If we use the Control Test, the legal fiction would make it appear that Company B is compliant, when in fact is it not as it is not fully or absolutely Filipino-owned.

It shall be understood that the foregoing opinion is rendered based solely on the facts disclosed in the query and relevant solely to the particular issues raised therein and shall not be used in the nature of a standing rule binding upon the courts, or upon the Commission in other cases of similar or dissimilar circumstances. If upon investigation, it will be disclosed that the facts relied upon are different, this opinion shall be rendered null and void.[4]

Please be guided accordingly.

CAMILO S. CORREA
General Counsel

[3] Executive Order No. 65 dated 29 October 2018
[4] SEC Memorandum Circular 2003-15, No.7