OFFICE OF THE GENERAL COUNSEL

05 November 2024

SEC-OGC Opinion No. 24-32
Re: Foreign Investments Act of 1991
Paid-in Capital

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Attention: **Atty. Dennis Arvin L. Chan**
Partner

Dear Atty. Chan:

This refers to your letter[1] requesting the Commission's opinion on whether the term "paid-in" capital under Section 8 of the Republic Act (RA) No. 7042 or the Foreign Investments Act of 1991 (FIA) includes additional paid-in capital (APIC), and whether such APIC can be converted to increase the "paid-up capital" of a corporation.

You stated in your letter that under Section 8 of the FIA, if small and medium-sized domestic market enterprises "xxx (1) [involve] advanced technology as determined by the Department of Science and Technology; or (2) [employ] at least fifty (50) direct employees, then a minimum **paid-in capital** of one hundred thousand US dollars (US 100,000.00)" shall be required in order for such domestic enterprises to have more than forty percent (40%) foreign equity.

You further averred that your client is a local corporation that employs more than fifty (50) direct employees with the following information:

Paid-up Capital	PhP4,500,000.00
Authorized Capitalization	PhP10,000,000.00
Additional Paid-in Capital	PhP10,000,000.00

In view thereof, you would like to request for the Commission's opinion on the following:

1. For purposes of complying with Section 8 of the FIA, does the term "paid-in capital" include APIC?; and
2. Assuming that the term "paid-in capital" does not include APIC, can a company convert or use a portion of its APIC to increase the paid-up capital?

[1] Letter dated 17 March 2021

FIA, as amended by RA No. 11647, and its Implementing Rules

Section 8 of the FIA, as amended[2], provides:

> "Section 8. List of Investment Areas Reserved to Philippine Nationals (Foreign Investment Negative List). - x x x
>
> Except as otherwise provided under Republic Act No. 8762, otherwise known as the Retail Trade Liberalization Act of 2000 and other relevant laws, micro and small domestic market enterprise with **paid-in** equity capital less than the equivalent of Two hundred thousand US dollar (US$200,000.00), are reserved to Philippine nationals: Provided, That if: (1) they involve advanced technology as determined by the Department of Science and Technology, or (2) they are endorsed as startup or startup enablers by the lead host agencies pursuant to Republic Act No. 11337, otherwise known as the Innovative Startup Act; or (3) a majority of their direct employees are Filipinos, but in no case shall the number of Filipino employees be less than fifteen (15), then a minimum **paid-in** capital of One hundred thousand US dollars (US$100,000.00) shall be allowed to non-Philippine nationals. xxx"

Rule XII, Section 39 (c) of the Implementing Rules and Regulations (IRR) of the FIA, as amended (FIA-IRR)[3], provides that micro and small domestic market enterprises, that are non-Philippine nationals, shall be allowed a minimum paid-in capital of US$100,000 or its equivalent, subject to the following:

i. They involve advanced technology as determined by the DOST;
ii. They are endorsed as startup or startup enablers by the lead host agencies, namely the Department of Trade and Industry (DTI) or Department of Information and Communications Technology (DICT) or Department of Science and Technology (DOST), pursuant to R.A. No. 11337, otherwise known as the Innovative Startup Act; or
iii. They execute a notarized undertaking that the majority of their direct employees shall be Filipinos and that in no case shall the number of Filipino direct employees be less than fifteen (15).

Provided, further, that the registered foreign enterprises employing foreign nationals and enjoying fiscal incentives shall develop and implement an understudy training program or skills development program to ensure the transfer of technology skills to Filipino employees within the same enterprise.

Rule I, Section 1 (hh) of the FIA-IRR, as amended, defines paid-in equity capital as:

> "**Paid-in equity capital** shall mean the total investment in a business that has been paid-in in a corporation or partnership or invested in a sole proprietor, which may be in cash or in property. It shall refer to inward remittance or assigned capital in the case of foreign corporations."

"Paid-up capital" and "paid-in capital"

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[2] Republic Act No. 11647, An Act Promoting Foreign Investments, Amending thereby Republic Act No. 7042, otherwise known as the "Foreign Investment Act of 1991", As Amended, and for Other Purposes, 02 March 2022.

[3] Implementing Rules and Regulations of Republic Act (RA) No. 11647or An Act Promoting Foreign Investments, Amending thereby Republic Act No. 7042, otherwise known as the "Foreign Investment Act of 1991", As Amended, and for Other Purposes, 11 July 2022.

The term ***paid-up capital*** was used in Section 13[4] of Batas Pambansa Bilang. 68 or the Corporation Code[5].

In *MSCI-Nacusip Local Chapter vs. National Wages and Productivity Commission et al.*[6], the Supreme Court said:

> "**By express provision of Section 13, paid-up capital is that portion of the authorized capital stock which has been both subscribed and paid.** To illustrate, where the authorized capital stock of a corporation is worth P1 million and the total subscription amounts to P250,000.00, at least 25% of this amount, namely, P62,500.00 must be **paid up** per Section 13. The latter, P62,500.00, is the **paid-up capital** or what should more accurately be termed as paid-up capital stock.
>
> xxx
>
> Not all funds or assets received by the corporation can be considered paid-up capital, for this term has a **technical signification** in Corporation Law. **Such must form part of the authorized capital stock of the corporation, subscribed and then actually paid.**" (Emphasis ours)

While Section 13 no longer appears in the Revised Corporation Code (RCC)[7] because minimum ***paid-up capital*** is no longer required upon incorporation, unless required by other special laws such as the FIA, the term and concept ***"paid-up capital"*** survives and is still applicable where capital stock is subscribed, and then subsequently paid, especially under the fourth (4th) paragraph of Section 37 of the RCC [8] relative to the increase of capital stock.

On the other hand, ***paid-in capital*** is defined under Section 2 of SEC Memorandum Circular No. 16 Series of 2023[9] as follows:

> "xxx **Paid-In Capital** – the sum of the amount paid for shares of stock issued, including the **additional paid-in capital (APIC) or premium** paid over the par value of shares." (Emphasis ours)

APIC "is any contribution of stockholders *over* the par value of shares. Incidentally, a share premium is also defined as the amount received by a firm over the par value of its share."[10]

Thus, ***paid-up capital*** differs from ***paid-in capital*** such that the former refers to shares actually subscribed and paid while the latter is the sum of the amount paid for shares of stocks issued, plus the APIC, or the excess or premium paid over the par value of such shares.[11]

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[4] "Section 13. Amount of capital stock to be subscribed and paid for the purposes of incorporation. - At least twenty-five percent (25%) of the authorized capital stock as stated in the articles of incorporation must be subscribed at the time of incorporation, **and at least twenty-five (25%) per cent of the total subscription must be paid upon subscription**, the balance to be payable on a date or dates fixed in the contract of subscription without need of call, or in the absence of a fixed date or dates, upon call for payment by the board of directors: **Provided, however, That in no case shall the paid-up capital be less than five Thousand (P5,000.00) pesos.**" (Emphasis ours)

[5] Batas Pambansa Blg. 68, The Corporation Code of the Philippines, 1 May 1980.

[6] G.R. No. 125198. March 3, 1997 citing Agbayani, Commentaries and Jurisprudence on the Commercial Laws of the Philippines, Vol. III, 1984 ed., p. 153.

[7] Republic Act No. 11232, The Revised Corporation Code of the Philippines, 20 February 2019.

[8] SEC. 37. Power to Increase or Decrease Capital Stock; Incur, Create or Increase Bonded Indebtedness. –

xxx " Provided, that the Commission shall not accept for filing any certificate of increase of capital stock unless accompanied by a sworn statement of the treasurer of the corporation lawfully holding office at the time of the filing of the certificate, **showing that at least twenty-five percent (25%) of the increase in capital stock has been subscribed and that at least twenty-five percent (25%) of the amount subscribed has been paid** in actual cash to the corporation or that property, the valuation of which is equal to twenty-five percent (25%) of the subscription, has been transferred to the corporation".xxx

[9] SEC Memorandum Circular No. 16, Series of 2023, Revised Guidelines on the Determination of Retained Earnings Available for Dividend Declaration, 19 September 2023.

[10] SEC Opinion No. 14-13 dated 11 June 2014 addressed to Isla Lipana & Co.

[11] SEC-OGC Opinion No.19-40 dated 16 September 2019 addressed to Mr. Jose Ma. L. Quiaoit.

Thus, we answer your **first query** in the **affirmative.**

As to your **second query**, we answer it in the **negative.**

It is already settled that the ***conversion*** of APIC involves the observance of the Trust Fund Doctrine.[12]

In *National Telecommunications Commission (NTC) v. Court of Appeals*[13], the Supreme Court discussed trust fund doctrine in relation to capital, thus:

> "The term "capital" and other terms used to describe the capital structure of a corporation are of universal acceptance, and their usages have long been established in jurisprudence. Briefly, **capital refers to the value of the property or assets of a corporation. The capital subscribed is the total amount of the capital that persons (subscribers or shareholders) have agreed to take and pay for, which need not necessarily be, and can be more than, the par value of the shares. In fine, it is the amount that the corporation receives, inclusive of the premiums if any, in consideration of the original issuance of the shares. In the case of stock dividends, it is the amount that the corporation transfers from its surplus profit account to its capital account. It is the same amount that can loosely be termed as the "trust fund" of the corporation. The "Trust Fund" doctrine considers this subscribed capital as a trust fund for the payment of the debts of the corporation, to which the creditors may look for satisfaction. Until the liquidation of the corporation, no part of the subscribed capital may be returned or released to the stockholder (except in the redemption of redeemable shares) without violating this principle.** Thus, dividends must never impair the subscribed capital; subscription commitments cannot be condoned or remitted; nor can the corporation buy its own shares using the subscribed capital as the consideration therefor."

In *Ong Yong et al vs. David S. Tiu, et al.*[14], the Supreme Court laid down the instances as to when the distribution of corporate Trust Fund is allowed, thus:

> The Trust Fund Doctrine, first enunciated by this Court in the 1923 case of *Philippine Trust Co. vs. Rivera*, provides that subscriptions to the capital stock of a corporation constitute a fund to which the creditors have a right to look for the satisfaction of their claims. **This doctrine is the underlying principle in the procedure for the distribution of capital assets, embodied in the Corporation Code, which allows the distribution of corporate capital only in three instances: (1) amendment of the Articles of Incorporation to reduce the authorized capital stock, (2) purchase of redeemable shares by the corporation, regardless of the existence of unrestricted retained earnings,and (3) dissolution and eventual liquidation of the corporation.** Furthermore, the doctrine is articulated in Section 41 on the power of a corporation to acquire its own shares and in Section 122 on the prohibition against the distribution of corporate assets and property unless the stringent requirements therefor are complied with.
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> The distribution of corporate assets and property cannot be made to depend on the whims and caprices of the stockholders, officers or directors of the corporation, or even, for that matter, on the earnest desire of the court *a quo* "to prevent further squabbles and future litigations" unless the indispensable conditions and procedures for the protection of corporate creditors are followed. Otherwise, the "corporate peace" laudably hoped for by the court will remain nothing but a dream because this time, it will be the creditors' turn to engage in "squabbles and litigations" should the court order an unlawful distribution in blatant disregard of the Trust Fund Doctrine." (Emphasis supplied)

In *Philip Turner et al., v. Lorenzo Shipping Corporation*[15], the Supreme Court reiterated *Ong Yong* when it held that:

> "There can be no distribution of assets among the stockholders without first paying corporate debts. Thus, any disposition of the corporate funds and assets to the prejudice of creditors is null and void.

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[12] Supra, Note 10; SEC OGC Opinion No. 19-50 dated 11 October 2019 addressed to Tan Venturanza Valdez
[13] G.R. No. 127937 July 28, 1999.
[14] G.R. No. 144476, April 8, 2003.
[15] G.R No. 157479, November 24, 2010.

Ownership of APIC belongs to the corporation which is considered part of its funds/assets, and there is no possible instance that APIC will be outside of the coverage of the term "paid-in capital". Be that as it may, granting ex gratia that APIC is not included in the term "paid-in capital", the fact that the law considers it as part of the assets of the corporation, it cannot possibly be converted or used to increase the paid-up capital as the same will be tantamount to the corporation using its own funds/assets to pay for the subscription of stockholders to facilitate the issuance of its own shares. This will clearly violate the trust fund doctrine.

It shall be understood, however, that the foregoing opinion is rendered solely on the basis of the facts and circumstances disclosed to the Commission, and should be considered relevant only to the particular issue raised therein. This opinion shall not be considered and used in the nature of a standing rule binding upon the Commission in other cases, or upon the courts whether of similar or dissimilar circumstances[16]. If, upon further inquiry or 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,

Romuald C Padilla
General Counsel

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