MBC CongressWatch Report
Towards Greater Voter Involvement

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Amending the Corporation Code

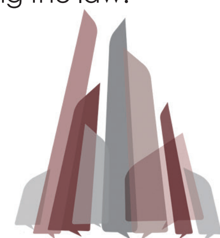
Following the enactment of two "business friendly" laws namely the Go Negosyo Act (Republic Act 10644) and the Philippine Competition Act (Republic Act 10667), Senator Bam Aquino, chairman of the Senate Committee on Trade, Commerce and Entrepreneurship sponsored another measure which aims to improve and develop the country's business regulatory practices for the benefit of local entrepreneurs. Senate Bill 2945, under Committee Report 247, now on Second Reading seeks to amend the 1980 law, Batas Pambasa Blg. (BP) 68, or the Corporation Code of the Philippines.

In his sponsorship speech last September 9, he stressed the need to update the 35-year old law "to catch up to global best practices for the business sector and improve the ease of doing business in the country." To do so, the bill provides for the creation of one-person corporations, allows perpetual corporate terms, grants additional powers to the Securities and Exchange Commission (SEC), and amends the structure of corporations for better governance.

One-person Corporation

Under the existing Corporation Code, any number of natural persons not less than five, but not more than 15, all of legal age and a majority of whom are residents of the Philippines, may form a private corporation for any lawful purpose or purposes.[1] On the other hand, solo entrepreneurs who wish to start a business will have to do so under a sole proprietorship. However, under this set-up, personal assets are considered property of the business entity; hence these can be subject to seizure in case of bankruptcy or in other liabilities. As a result, there have been instances where "dummy incorporators" have been used to avoid the sole proprietorship structure, effectively circumventing the law.

To address this, the bill proposes the creation of a one person corporation (OPC) as an alternative to sole proprietorship. Under an OPC, the properties of the individual and the corporation are made separate and independent of each other. An OPC shall have only one director or trustee. It also requires the payment in one lump sum of the minimum authorized capital stock. Further, it provides that there should be no other OPC wherein the individual is the sole stockholder.



The establishment of OPCs is a welcome development for business enthusiasts. However, some private sector groups suggest that the P1 million paid up capital for OPCs [even for small corporations] may be too high and may discourage applicants, considering that regular corporations may actually have a lower paid up capital of P62,500. It was also recommended to reconsider the prohibition on multiple one person corporations by an individual. For its part, the SEC believes that the capital requirement demonstrates the seriousness of the individual in setting up the business. Moreover, the Commission would rather gain experience first on regulating OPCs before allowing an individual to establish more than one OPC even for different business purposes.

The measure specifies additional provisions governing OPCs:

- The words "one person corporation" or the letters "OPC" shall be displayed either below or at the end of the corporate name wherever printed, affixed, engraved or otherwise presented
- While no stockholder's meeting is required, resolutions and decisions shall be valid when they are written, signed, and dated by the single stockholder or director and when recorded in the minutes-book of the OPC
- There is a presumption of co-mingling as the single stockholder shall assume joint and several liability if he cannot prove that the property of the OPC is independent of his or her own property
- OPCs can be converted into a regular stock corporation. Conversely, a regular stock corporation can, likewise, apply for conversion into a one person corporation

Perpetual Corporate Term

According to the SEC, perpetual existence for corporations will be the rule and limited terms the exception. The bill provides that a corporation with a perpetual term or a term exceeding 25 years shall be subject to a periodic review by the Commission. The same shall be required to comply with renewal requirements every 25 years. Failure to do so will not terminate the corporation's existence, but the Commission shall impose penalties and withhold action on requests and applications before the SEC until full compliance is made.

For certain sectors, however, renewal every 25 years seem contrary to the idea of perpetuity. Corporations may require more time from initial market penetration in order to develop long-term sustainable plans and achieve their socio-economic goals. Twenty-five years may be too short a time and burdensome to business entities to churn out renewal requirements. It will also mean belabouring government agencies that will have to frequently accommodate companies trying to comply with reportorial requirements.

Interestingly, the current law actually requires renewal every 50 years. The SEC however, gives more emphasis on the need to better monitor corporations. To illustrate, according to the Commission, only about 200,000 of the 900,000 registered corporations have submitted their 2014 Audited Financial Statements as of June 2015.

Facilitating corporate operations

In his explanatory note in Senate Bill 2194, his version of the Amendments to the Corporation Code, Senator Sonny Angara noted that the name verification process will be simplified, electronic submissions and notices will be accepted, and the SEC will be authorized to develop or employ new systems such as online registration. The same provisions are found in the consolidated bill sponsored by Senator Aquino.

Specifically, it prescribes guidelines for the SEC in the registration and incorporation of companies, and the commencement of corporate existence. The process starts with the verification of the intended corporate name whether it is distinguishable from other names already reserved or registered by other existing corporations. Once established, all directors or trustees have the express duty to attend all meetings. They may also be allowed to attend meetings through remote communication and to vote in absentia. The articles of incorporation and by-laws or amendments thereto may also be filed and submitted electronically.

In addition, the proposed law provides for expanded methods and procedures for dissolution. It provides instances when the assets of the dissolved corporations may be forfeited.

Meanwhile, relief measures are extended to "troubled" businesses. The measure allows a corporation whose term has expired or lapsed within 10 years prior to the effectivity of the law to apply for the "revival" of its certificate of incorporation. It also extends the period of non-operation to five years from the previous two years from the date of incorporation before the corporation's certificate of incorporation may be deemed revoked. For corporations that commenced operations, but subsequently became inoperative for at least five consecutive years, the Commission may not automatically suspend or revoke the entity's certificate of incorporation. The Commission can instead place the company under delinquency status, where it will have the opportunity to comply with SEC requirements and payment of fines and penalties.

More regulatory policies

To facilitate the conduct of corporate affairs, the proposed bill allows SEC to motu propio or upon application by a stockholder, member, director or trustee to order the conduct of elections. Failure to conduct any elections and its reasons shall be reported to the Commission within 10 days from the date of the schedule. The report shall further state the new schedule of the elections which shall be within 30 days from the original date.

It also specifies a particular schedule when a cessation from office of directors, trustees, or officers shall be reported, which is within three days from cessation. Moreover, the filing of the application for any increase or decrease in the capital stock shall be within three months from the date of the approval by the board of directors and stockholders.

There have been reservations with regard to the prescribed periods as being too tight for compliance. The Commission however, maintains that the time element is crucial, since the delays in the

holding of elections are usually the precursor of disputes. With regard to increasing or decreasing capital stock, since it reflects the financial stability of the corporation and affects the behavior of stockholders, it is important that such action be communicated and implemented within the prescribed period.

Similarly, there are additional regulatory requirements which may seem to belabor corporations. There is a provision that requires the inclusion of specific items in the corporation's by-laws which are otherwise only recommendatory under the current law. These include the following:

- The time and manner by which accurate and timely information shall be given to stockholders
- Code of ethics or standards of conduct in dealing with government instrumentalities, including mechanisms by which it will be enforced
- Internal procedures governing reports by whistleblowers during and after employment
- A system for monitoring compliance with the rules and regulations on good corporate governance including the appointment of a compliance officer

The same observation goes to the provisions prescribing detailed contents in the notices and agenda of regular and special stockholders meetings, including the minutes of the previous one. It is suggested, however, that some pieces of information are best introduced through SEC regulatory issuances rather than being required in the proposed bill. This would allow more flexibility for amendments in the future.

Another regulatory feature in the proposed amendments is the provision on de facto mergers. The sale of the assets of a corporation shall be deemed a merger or consolidation when the buyer and seller corporations engage in the same or similar business, whether whole or in part, and the transaction:

- Is a sale of all or substantially all of the assets of the corporation
- Results in the cessation of the seller's ordinary business or a prohibition to engage in the same
- Involves the integration of the seller assets and operations into the buyer's own business
- Has the buyer assuming the seller's liabilities
- Consists of the payment with the buyer's own stock
- Prohibits the seller from continuing or engaging in the same or similar business

The authority of the corresponding regulatory agencies is still recognized, particularly those overseeing banks, trust and insurance companies, public utilities, educational institutions, and other kinds of corporations governed by special laws, wherein a favorable recommendation is necessary in getting the SEC's approval. At present, application for mergers, after having found compliant with SEC requirements is endorsed to the DOJ-Office for Competition for evaluation. With the recent enactment of the Competition Law, which establishes the Philippine Competition Commission, the process on mergers and consolidation may have to be reviewed.

Better corporate governance

To ensure good corporate governance, or when public interest so dictates, the Commission is authorized to require the formation of special committees within corporations, to whom the SEC can designate their powers and functions. The term of office and the compensation of the committee members, however, are to be determined by the board, with the corporation's by-laws amended accordingly within the prescribed period.

Corporations imbued with public interest, as may be defined by the Commission, are required to have at least one independent director. There shall also be an appointed compliance officer who will report directly to a compliance committee composed of at least three directors. There is an issue, however, on whether this should also apply to one person corporations and small corporations. The measure provides that an OPC will have only one director, while small corporations (with total assets worth more than P3 million but not more than P15 million) may have two or three incorporators.

The introduction of the concept of small corporations in the proposed bill seems to have no counterpart in other economies as to merit differentiation. The delineation is either between being a listed or non-listed company, either domestic or foreign, and whether a company will operate as a public utility or a closed corporation. Under Republic Act 9501, or the Magna Carta for Micro, Small and Medium Enterprises, MSMEs are categorized by asset size and by employment size. For small enterprises, the assets should be above P3 million to P15 million, or that the number of employees range from 10 to 99 workers.

Regardless of size, directors, trustees and officers of a corporation shall adhere to specific standards and principles, including the circumstances for disqualification. A person is disqualified from being elected as a director when:

- Convicted by final judgment of an offense punishable by imprisonment for a period exceeding six years, or violation of the Corporation Code, as well as the Securities Regulation Code within five years prior to election or appointment
- Convicted by final judgment or found administratively liable for fraud and other related crimes whether by a local or foreign authority
- Convicted by final judgment for repeated offenses regardless of when committed
- An independent director sits in the board of more than five corporations

Fit and proper rule

To complement the above rules, Finance Secretary Cesar Purisima issued the adoption of guidelines prescribing the fit and proper rule for directors of insurance companies and public companies.[1] The Insurance Commission and SEC, both under the administrative supervision of the Department of Finance are instructed to promulgate guidelines and implement a system of ranking companies to ensure that directors are fit and proper to hold such position. The guidelines include criteria on integrity, experience, education, training, and competence.

[1] *DOF Department Order 54-2015 issued 15 April 2015.*

It sets the ideal minimum qualification of a director:

- At least 25 years old at the time of election or appointment
- At least a college graduate or has at least five years business experience
- Has attended a special seminar on corporate governance for board directors conducted or accredited by the SEC or the Insurance Commission
- Must be fit and proper for the position taking into account the following: integrity or probity, competence, relevant education and training, physical and mental fitness, diligence, and knowledge and experience

It also prescribes a minimum qualification for, and an ideal minimum number of independent directors. They shall be at least 20% but not less than two members of the board of directors. For publicly-listed corporations, the number shall be proportionate to the percentage of shares held by the public.

Moreover, the issuance provides for the ideal tenure of an independent director to be five consecutive years. After the completion of the term, the director shall be considered ineligible for re-election until after the lapse of the "cooling period" of two years. When the two-year prohibition expires, he or she may be elected for another five-year term. Upon finishing the cumulative period of ten years, the same shall be perpetually barred from being elected in the same covered entity.

The proposed bill in the Senate further provides that the maximum number of board representations of any independent director or trustee shall be limited to five corporations.

Certain sectors meanwhile believe that independence and competence of directors are not necessarily reflected by the mere number of seats held, or on the length of service, or just by sheer age. Independent directors can also be held accountable through the submission of independent reports that would indicate their attendance and participation in corporate meetings and events.

Corporate liability

Accountability is likewise exacted from the board of directors and officers, especially for criminal offenses. The current Corporation Code does not have a definitive clause that specifies crimes to be penalized on the part of the corporation; it merely suggests that criminal charges are the sole responsibility of the company's executive management. The Supreme Court is also of the view that criminal penalties cannot be imposed on companies but rather on the directors or officers responsible for the violation.

The proposed amendments impose sanctions not only on the upper management, but also on the corporation as a legal entity that is supposed to act maturely and lawfully. The Commission then is empowered to act on a complaint or to initiate an investigation to determine whether a violation has been committed or "is about" to be committed. It is likewise authorized to administer oaths, issue subpoena and cease and desist orders, even to cite a person in contempt.

Administrative sanctions include a fine ranging from P5,000 to P2 million, and arrest and detention. Companies can also face suspension or revocation of their certificates of incorporation, dissolution and forfeiture of assets. The bill lists crimes and corresponding penalties for the following acts:

- Continued and unjustified use of former corporate name
- Concealment of disqualification
- Violation of duty to keep or maintain records and allow their inspection or reproduction
- Knowing or willful certification of incomplete, inaccurate, false or misleading statement or reports
- Collusion of independent auditors
- Fraudulent procurement by the organization
- Fraudulent or unlawful conduct of business
- Identity theft
- Acting as intermediaries or engaging with intermediaries for graft and corrupt practices
- Tolerating graft and corrupt practices
- Retaliation against whistleblowers

During MBC's roundtable meeting with SEC Chair Teresita Herbosa last 1 December 2014, the issue on criminal liability and penalties was raised if such could be reduced. As it is, some individuals are hesitant to take on the directorship position or even as a corporate secretary due to the risks tied to it.

Nevertheless, the measures are seen to further promote good corporate governance by including stricter measures to safeguard companies from being used for instances of fraud, graft, and corruption. Ultimately, this necessary upgrade is actually an effort to meet international standards set by the United Nations Convention Against Corruption (UNCAC), an international multilateral agreement where the Philippines is a party to. The Chair further stressed that the provisions on criminal liability are aligned with the practices of other countries.

Balancing reforms

According to the World Economic Forum and World Bank, corruption adds up to 10% of the total cost of doing business in many parts of the world, and up to 25% of the cost of procurement contracts in developing countries where most ASEAN countries are classified. It distorts market mechanisms, prevents fair competition, exposes businesses to legal and reputational risks, and erodes public investor trust and confidence.[2]

While there is an intensive global call for the government to once and for all address this impasse, there is also an equal demand for the private sector to participate and even devise their own means to supplement efforts to combat unethical business practices. The Makati Business Club, for its part, responds to the challenge through the Integrity Initiative, a private sector-led campaign that aims to initiate collective action among ethical foreign and local business enterprises towards clean business practices. Ultimately, the goal is to establish a certification and accreditation system, like the ISO, that will provide competitive advantages to compliant companies. Companies will be

[2] *ASEAN CSR Network. Business and Anti-Corruption Model*

audited, accredited, and certified based on compliance to ethical ways of doing business and strict integrity standards.

Corporations have now ceased to become merely profit-oriented entities whose sole purpose is to generate economic value for private interests. They are considered critical partner of the government in nation building towards a more sustainable and inclusive growth.

Thus, it is the prime responsibility of the government to develop mechanisms and policies to enhance the ease of doing business and improve corporate governance for investor protection. Indeed, the proposed amendments to the Corporation Code are meant to address unethical business practices and private sector corruption. However, while the SEC articulately states that the focus of attention should not be on added expense, but rather more on “adding value” in terms of a better reputation for good governance, due consideration should also be placed on governance measures that will stimulate business activity, rather than hamper it with overly cautious regulations.

Moreover, during the congressional hearing, the Commission stresses that the amendments introduced are intended to improve the standing of Philippine companies in the ASEAN Corporate Governance Scorecard (ACGS). While benchmarking is the norm in this globalized economy, there may be necessary measures that are intrinsic to the Philippines, given our own market structure, as well as customs and practices which require specialized rules and procedures.

ACGS was introduced in 2011 under the ASEAN Capital Market Forum to harmonize rules and regulations to achieve greater integration of the region’s capital markets. The tool assesses the corporate governance performance of publicly listed companies in the ASEAN-6 (Indonesia, Malaysia, Philippines, Singapore, Thailand, and Vietnam) against international best practices.

The counterpart version of SB 2945 in the House of Representatives, House Bill 4407 is pending in the committee on Trade and Industry. Meanwhile, the principal author of the bill, Rep. Mel Senen Sarmiento was recently sworn in as the DILG chief succeeding former Sec. Mar Roxas. Hence, the chances of its passage in the current Congress slim especially in the House with the priority given to the Bangsamoro Basic Law and the General Appropriations Act. If the Senate can squeeze consideration of the measure despite the BBL, and the national budget likely to drag in the plenary, approval on third reading of the measure is possible.

It is therefore important to be ready with the acceptable provisions and finalized version when the bill gets fast-tracked anytime before February 2016, when the “official” start of the campaign season kicks in.

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