Republic of the Philippines
Department of Finance
Securities and Exchange Commission

OFFICE OF THE GENERAL COUNSEL

SEC-OGC Opinion No. 16-16
Minimum Stock Subscription and
Treasury Shares

27 June 2016

MA. FENORA L. PIGON
Vice President for Finance
Antonino Group of Companies
17th Floor, G.E. Antonio Building,
J. Bocobo St., cor TM Kalaw St.,
1000 Ermita, Manila

Madam:

This refers to your letter dated February 24, 2016 requesting for an opinion regarding minimum stock subscription and treasury shares.

You stated in your letter that Company A has an authorized capital stock of Two Million Seven Hundred Fifty Thousand Pesos (P2,750,000.00) divided into Twenty Seven Thousand Five Hundred (27,500) shares of stock with par value of One Hundred Pesos (P100.00) per share, of which Seven Million Eight Hundred Ten Thousand Seven Hundred Sixty Four (7,810,764) shares or 28.4028% are subscribed.

According to you, Company A bought out three (3) of its shareholders which, many argued, has effectively reduced the subscribed capital stock to 15.8127% or less than the 25% minimum capital stock that is required to be subscribed, pursuant to Section 13 of the Corporation Code. The subject treasury shares were not reported or recorded in the balance sheet of the corporation.

Thus, your queries:

1. Under the circumstances, may Company A treat the treasury shares as part of issued shares?

2. Because of its buy-back program, did Company A violate Section 13 of the Corporation Code on minimum stock subscription?

3. Considering that Company A is now planning to make available for subscription/sale said treasury shares, can it sell the same directly without having to ask the SEC for exemption from the registration requirements of the Revised Securities Code?

4. Can Company A merely amend its audited financial statements (particularly its balance sheet) and indicate therein the treasury shares?

Before we address your queries, we discuss first the nature of treasury shares.

Section 9 of the Corporation Code defines treasury shares as:

> "SEC. 9. Treasury Shares. Treasury shares are shares of stock which have been issued and fully paid for, but subsequently reacquired by the issuing corporation by

purchase, redemption, donation, or through some other lawful means. Such shares may again be disposed of for a reasonable price fixed by the board of directors."

In other words, treasury shares are shares that have been earlier issued and are regarded as property acquired and currently owned by the corporation and not by any of its stockholders.[1] Being the owner of treasury shares, the corporation may opt to retire, sell or distribute as property dividends said shares.[2]

Thus, we answer your first query in the affirmative. Company A may treat the treasury shares as part of the issued shares as long as they are not cancelled or retired. Treasury shares do not revert to the unissued shares of a corporation but are regarded as property acquired by the corporation which may be reissued or resold by the corporation at a price to be fixed by the Board of Directors.[3] Since treasury shares do not revert back to unissued shares, they do not lose their status as "issued shares."[4] When outstanding shares are acquired in treasury, their issued status is not disturbed. These are still part of the issued capital stock although no longer outstanding[5]. This is so because the amount paid for the acquisition of treasury shares does not represent return of capital to the stockholders but an investment out of retained earnings on a salable property known as treasury shares.[6]

As to your second query, we answer the same in the negative. Section 13[7] of the Corporation Code mandates pre- incorporation subscriptions, which means that at least 25% of the amount of authorized capital stock shall be subscribed at the time of incorporation and at least 25% of the total subscription must be paid except where the capital stock consists of no par value shares, in which case, the subscription must be fully paid.[8]

The above "25% and 25%" requirement are **mandatory ONLY** during (1) **pre incorporation period** (Sec. 13); and (2) when the corporation undertakes to increase its authorized capital stock. The acquisition of treasury shares does not reduce the number of issued shares or the amount of stated capital and their "sale" does not increase the number of issued shares or the amount of stated capital.[9] Thus, the redeemed shares (treasury shares) are still part of the total shares of stocks issued to subscribers or stockholders whether or not fully paid or partially paid but no longer outstanding.[10]

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[1] SEC-OGC Opinion No. 06-12 dated April 20, 2012 addressed to Rosalino L. Marable.
[2] *Id.*
[3] SEC-EAD Opinion on Accounting for Treasury Shares (No date supplied);SEC Rules Governing Redeemable and Treasury Shares [CCP] No. 1-1982.
[4] SEC-OGC Opinion dated 22 June 1995 addressed to Mr. Edward S. De Los Reyes.
[5] Commissioner of Internal Revenue v Manning; 66 SCRA 14 (1975); Section 137, Corporation Code.
[6] *Supra* note 3.
[7] The Corporation Code.

> Sec. 13. Amount of capital stock to be subscribed and paid for the purposes of incorporation. -At least twenty -five percent (25%) of the subscribed capital as stated in the articles of incorporation must be subscribed at the time of incorporation, and at least twenty five (25%) 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 (5000) pesos.

[8] R. Lopez ,The Corporation Code of the Philippines 1st Ed., p.175.
[9] SEC-OGC dated January 14, 1993 addressed to Imelda P. Maiquez.
[10] H. De Leon, The Corporation Code of the Philippines, 2002 Ed, p.104.

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On your third query, Section 8.1 of the Securities Regulation Code (SRC)[11] provides that "[s]ecurities shall not be sold or offered for sale or distribution within the Philippines, without a registration statement duly filed with and approved by the Commission. Prior to such sale, information on the securities, in such form and with such substance as the Commission may prescribe, shall be made available to each prospective purchaser". This is practically the same requirement under the Revised Securities Act (RSA), which was repealed by the SRC.

In one Opinion,[12] which still holds true pursuant to the provisions of the SRC, the Commission held that:

> "[Re-issuance of treasury shares] is subject to the provisions of the Revised Securities Act (RSA), considering that the re-issuance thereof may constitute distribution of securities to the public, and consequently, new or additional stockholders may come in. Under Section 4 of the RSA,[13] no securities (which include shares of stocks), except that of a class exempt under any of the provisions of Section 5[14] thereof or unless sold in any transaction exempt under any of the provisions of Section 6[15] thereof, shall be sold or offered for sale or distributed to the public unless such securities shall have been registered and permitted to be sold or distributed. **However, while the re-issuance of treasury shares is not exempt per se under Sections 5 and 6 of said Act**, the same may be exempted from registration requirements considering that said transaction is of limited character as the corporation does not normally acquire its own shares of stocks and the number of shares to be disposed of is usually minimal. However, exemption thereof is not automatic. The corporation is still required to secure exemption from the Commission prior to such re-issuance pursuant to Section 6(b)[16] of the RSA."

On your last query, we answer the same in the affirmative. Company A should amend its audited financial statements to indicate the treasury shares with proper disclosure as to amendment. The Commission has opined that any declaration and issuance of treasury shares as property dividend shall be disclosed and properly designated as property dividend in the books of the corporation and in its financial statements.[17]

This Opinion is based solely on the facts disclosed in the query and relevant to the particular issues raised therein and shall not be used in the nature of a standing rule binding upon the Commission whether of similar or dissimilar circumstances.[18] If, upon investigation, it will be disclosed that the facts relied upon are different, this opinion shall be rendered void.

Please be guided accordingly.

CAMILO S. CORREA
General Counsel

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[11] Republic Act 8799 (2000).
[12] *Supra* note 9.
[13] Now Section 8 of SRC.
[14] Now Section 9 of SRC.
[15] Now Section 10 of SRC.
[16] Now, Section 10.2 of SRC.
[17] *Supra* note 1 citing SEC Rules CCP No. 1 (April 26, 1982), entitled "Rules Governing Redeemable and Treasury Shares," Section 5 (3).
[18] SEC Memorandum Circular No. 15, Series of 2003.