Republic of the Philippines
Department of Finance
Securities and Exchange Commission

OFFICE OF THE GENERAL COUNSEL

24 June 2019

SEC-OGC Opinion No. 19-24
Re: Foreign ownership requirement of partly nationalized activity

Atty. Dennis R. Quiokeles
Corporate Secretary
Green Earth Enersource Corporation
4/F Northside Business Hub,
G. Lopez Jaena, AP Cortes St., Tipolo
Mandaue City, Cebu 6014

Dear Atty. Quiokeles:

We write in response to your letter dated 27 March 2019 requesting an opinion on whether Green Earth Enersource Corporation (GEEC) complied with the ownership requirement under Section 2, Article XII of the 1987 Constitution.

You disclosed that GEEC is applying for the conversion of its Provisional Authority to Operate (PAO) into a Certificate of Compliance for its Buluan Biomass Power Plant as a FIT-eligible plant with rated capacity of 3.33 MW located in Brgy. Poblacion, Buluan, Maguindanao. The Energy Regulatory Commission (ERC), during its deliberation on the issue of GEEC's compliance with the 60%-40% Filipino-foreign ownership requirement under the Constitution and the Renewable Energy Act of 2008[1] (REA), directed GEEC to secure a formal Securities and Exchange Commission (SEC) opinion regarding its compliance. Hence, this request.

[1] Republic Act (RA) No. 9513

I. RULES ON CORPORATE NATIONALITY

Section 2, Article XII of the 1987 Constitution provides that "the exploration, development, and utilization of natural resources shall be under the full control and supervision of the State. The State may directly undertake such activities, or it may enter into co-production, joint venture, or production-sharing agreements with Filipino citizens, or corporations or associations at least sixty per centum (60%) of whose **capital** is owned by such citizens."

This is implemented by the REA which provides that Foreign Renewable Energy (RE) Developers may also be allowed to undertake RE development through an RE Service/Operating Contract with the government, subject to Article XII, Section 2 of the Philippine Constitution.[2]

Pursuant to this Constitutional foreign equity restriction, exploration, utilization and development of natural resources were placed under List A, Item 16 of the 11th Foreign Investment Negative List (FINL)[3], wherein only up to 40% foreign equity is allowed.

With respect to corporations, the Foreign Investment Act (FIA) of 1991[4] deems one to be a "Philippine national" if it is organized under the laws of the Philippines of which at least 60% of the capital stock outstanding and entitled to vote is owned and held by citizens of the Philippines.[5]

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[2] **RULE 6**

Regulatory Framework for the Renewable Energy Industry

SECTION 19. *Renewable Energy Service/Operating Contract.* —

A. *State Ownership of All Forces of Potential Energy*

All forces of potential energy and other natural resources are owned by the State and shall not be alienated. These include potential energy sources such as kinetic energy from water, marine current and wind; thermal energy from solar, ocean, geothermal and biomass.

B. *Parties to a Service/Operating Contract*

The exploration, development, production, and utilization of natural resources shall be under the full control and supervision of the State.

The State may directly undertake such activities, or it may enter into co-production, joint venture or co-production sharing agreements with Filipino citizens or corporations or associations at least sixty percent (60%) of whose capital is owned by Filipinos. Foreign RE Developers may also be allowed to undertake RE development through an RE Service/Operating Contract with the government, subject to Article XII, Section 2 of the Philippine Constitution.

[3] Executive Order No. 65, Promulgating the Eleventh Regular Foreign Investment Negative List.

[4] R.A. No. 7042

[5] Section 3, Republic Act No. 7042, Foreign Investments Act. Approved on 13 June 1991.

A. Base of 60%-40% Under Jurisprudence and SEC Memorandum Circular No. 8, Series of 2013

In the case of *Gamboa vs. Teves,* [6] the Supreme Court ruled that the "term 'capital' in Section 11, Article XII of the 1987 Constitution refers only to shares of stock entitled to vote in the election of directors, and thus in the present case only to common shares, and not to the total outstanding capital stock (common and non-voting preferred shares)."

Pursuant to this, the Commission issued **SEC Memorandum Circular No. 8, Series of 2013** (SEC-MC No. 8) which was upheld by the Supreme Court in *Roy v. Herbosa.*[7] SEC-MC No. 8 uses the two-tiered test in determining compliance with the required percentage of Filipino ownership. **Under the two-tiered test, the 60% required Filipino ownership shall be applied to BOTH: (a) the total number of outstanding shares of stock entitled to vote in the election of directors; AND (b) the total number of outstanding shares of stock, whether or not entitled to vote in the election of directors.**

B. Control Test vs. Grandfather Rule

In the Philippines, there are two acknowledged tests in determining the nationality of a corporation which has corporate stockholders: (i) the Control Test and (ii) the Grandfather Rule.

The Control Test states that shares belonging to corporations at least sixty percent (60%) of the capital of which is owned by Filipino citizens shall be considered as of Philippine nationality. **Under this test, there is no need to further trace the ownership of the 60% (or more) Filipino stockholdings of an investing corporation since a corporation which is at least 60% Filipino-owned is already considered as Filipino.**[8]

On the other hand, the Grandfather Rule is "the method by which the percentage of Filipino equity in a corporation engaged in nationalized and/or partly nationalized areas of activities, provided for under the Constitution and other nationalization laws, is computed, in cases where corporate shareholders are present, by *attributing* the nationality of the second or even subsequent tier of ownership to determine the nationality

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[6] *Heirs of Gamboa v. Teves*, G.R. No. 176579, 28 June 2011.

[7] *Jose M. Roy III v. Chairperson Teresita Herbosa*, G.R. No. 207246, 22 November 2016.

[8] *Narra Nickel Mining and Development Corporation, et. al. v. Redmont Consolidated Mines Corporation*, G.R. No. 195580, 21 April 2014, citing DOJ Opinion No. 020, series of 2005.

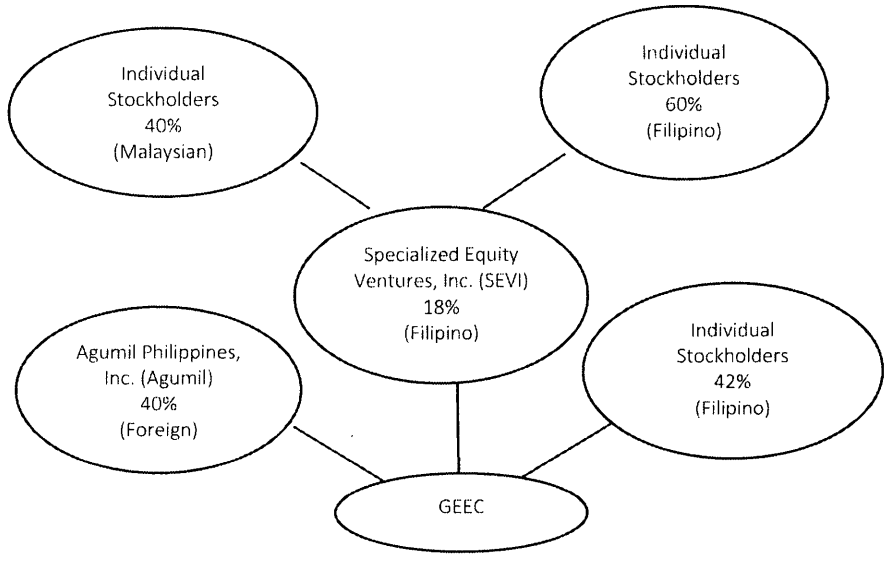
of the corporate shareholder."[9] Under this Rule, the Filipino ownership of the investing corporation and the investee corporation are combined to determine the percentage of Filipino ownership.

Please note that the Grandfather Rule is only applicable when the 60-40 Filipino-foreign equity ownership is in "doubt." For instance when the investing corporation has less than 60% Filipino stockholdings and the investee corporation has either 60-40% Filipino-foreign ownership ratio or is less than 60% Filipino. "Doubt", however, is not limited to these circumstances.

The Supreme Court, in its Resolution in *Narra Nickel Mining and Development Corporation v. Redmont Consolidated Mines, Corp., et al.,*[10] explained that even if the 60-40 Filipino to foreign equity ratio is apparently met by the investing or investee corporation, a resort to the Grandfather Rule is necessary if doubt exists as to the locus of the "beneficial ownership" and "control." The "doubt" refers to, "various indicia that the 'beneficial ownership' and 'control' of the corporation do not in fact reside in Filipino shareholders but in foreign stakeholders."[11]

II. DISCUSSION: USING THE TWO-TIERED TEST OF SEC-MC NO. 8

Based on the latest General Information Sheet (GIS) of GEEC which you attached to your letter, the ownership structure of the corporation is illustrated below:



[9] *Ibid, citing Narra Nickel Mining*
[10] *Ibid.*
[11] *Id., at Note 9.*

To determine whether the ownership structure of GEEC conforms with the foreign ownership restriction, the nationality of the above-mentioned stockholders (i.e. Agumil, SEVI, and "Individual Shareholders") must first be determined.

A. Nationality of SEVI

The latest GIS and Articles of Incorporation of SEVI on file with the Commission show an authorized capital stock of Php 1,000,000.00 divided into 1,000,000 common shares with a par value of Php 1.00 per share.

Since all shares are common shares (i.e. shares with voting rights), which thus comprise the totality of the Outstanding Capital Stock (OCS), it is sufficient to base the 60-40% requirement on the same to determine the nationality in compliance with SEC MC No. 8.

Based on its latest GIS on file with the Commission, all stockholders of SEVI are natural persons, as follows:

Name	Nationality	Number of Shares Subscribed	Amount Subscribed	Percent of Ownership
Lim Chan Lok	Malaysian	400,000	400,000.00	40.00%
Apolinar Y. Saso	Filipino	200,000	200,000.00	20.00%
Jonathan Furog	Filipino	200,000	200,000.00	20.00%
Gideon M. Sequiño	Filipino	100,000	100,000.00	10.00%
Yumiko U. Bajade	Filipino	100,000	100,000.00	10.00%

Since the shareholders of SEVI are all natural persons, it is no longer necessary to use either the Control Test or the Grandfather Rule as these tests are used to determine the nationality of a corporation (in this case, GEEC) only when it has an investing corporation (in this case, SEVI) that, in turn, has corporate stockholders. As SEVI's shares are 60% owned by individual Filipino citizens, SEVI is considered a Philippine National. Consequently, its 18% direct shareholding in GEEC is Filipino.

B. Nationality of Agumil

The latest GIS and Articles of Incorporation of Agumil on file with the Commission show an authorized capital stock of Php 650,000,000.00 divided into 6,500,000 common shares with a par value of Php 100.00 per share.

Since all shares are common shares (i.e. shares with voting rights), which thus comprise the totality of the OCS, it is sufficient to base the 60-40% requirement on the same to determine the nationality in compliance with SEC MC No. 8.

Based on the latest GIS on file with the Commission, Agumil is 100% owned by Agusan Plantations, Inc. which is 100% foreign-owned. Thus, Agumil's 40% direct shareholding in GEEC is foreign-owned.

C. Nationality of Individual Shareholders

Apart from Agumil and SEVI, all other shareholders of GEEC are natural persons, owning 42% of GEEC. The GIS of GEEC attached to your letter shows the following individual stockholders:

Name	Nationality	Number of Shares Subscribed	Amount Subscribed	Percent of Ownership
Ibrahim Gaguil Mangudadatu	Filipino	63,224,998	63,224,998.00	30.00%
Reynold Siy	Filipino	17,542,821	17,542,821.00	8.00%
Harry Ong	Filipino	8,545,171	8,545,171.00	4.00%
Lim Chan Lok	Malaysian	1	1.00	0.00%
DJ Parok D. Mangudadatu	Filipino	1	1.00	0.00%

Collectively, the "Individual Shareholders" are 100% Filipinos. Thus, their 42% direct shareholding in GEEC is Filipino-owned.

D. Nationality of GEEC

The Articles of Incorporation of GEEC on file with the Commission shows an authorized capital stock of Php 400,000,000.00 divided into 400,000,000 common shares with a par value of Php 1.00 per share.

Similar to SEVI and Agumil, since all shares of GEEC are common shares (i.e. shares with voting rights), which thus comprise the totality of the OCS, it is sufficient to base the 60-40% requirement on the same to determine the nationality in compliance with SEC MC No. 8.

From the foregoing, 60% of GEEC is held by Filipinos, as shown below; hence, GEEC complied with the ownership requirement under Section 2, Article XII of the 1987 Constitution.

Name	Nationality	Number of Shares Subscribed	Amount Subscribed	Percent of Ownership
Specialized Equity Ventures, Inc.	Filipino	37,137,007	37,137,077.00	18.00%
Individual Shareholders	Filipino	63,224,998	63,224,998.00	42.00%
Total Filipino Equity				60.00%

It shall be understood that the foregoing opinion is rendered based solely on the facts disclosed in the query as well as documents filed with the Commission by the requestor as part of its regular reportorial compliance, 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.[12] If upon investigation, it will be disclosed that the facts relied upon are different, this opinion shall be rendered null and void.

CAMILO S. CORREA
General Counsel

[12] SEC Memorandum Circular 2003-15, No. 7.