

## CHAPTER 8

### INVESTMENTS LAW

The Omnibus Investment Code of 1987 and the Foreign Investments Act of 1991<sup>1</sup> govern investments and the granting of incentives which are administered by the Department of Trade and Industry (DTI) through the Board of Investments (BOI) or the Philippine Economic Zone Authority (PEZA), together with all the laws regulating the making of investments or doing business by foreigners in the Philippines. It gives foreign and local investors complete information on all incentives which they may avail of, alternative investment schemes available to them and requirements for registration of foreign investments without incentives. Foreign investments mean equity investments made by a non-Philippine national, in the form of foreign exchange and/or other assets actually transferred to the Philippines and duly registered with the Central Bank which shall assess and appraise the value of such assets other than foreign exchange.<sup>2</sup>

The State encourages private domestic and foreign investments in industry, agriculture, mining, forestry, tourism, and other sectors of economy which shall: (1) provide significant employment opportunities relative to the amount of capital invested; (2) increase productivity of land, minerals, forestry, aquatic and other resources of the country and improve utilization of products thereof; (3) improve technical skills of people employed in enterprise; (4) provide foundation for future development of economy; (5) meet tests of international competitiveness; (6) accelerate development of less developed regions of country; and (7) result in increased volume and value of exports for economy. The State shall encourage projects which will contribute to attainment of these objectives, fiscal incentives without which said projects may not be established in locales, number and/or pace required for optimum national economic development. Fiscal incentive systems shall be devised to compensate for market imperfections, reward performance contributing to economic development, and be cost-efficient and simple to administer. Fiscal incentives shall be extended to stimulate investment and assist initial operations of enterprise, and shall terminate after a period of not more than 10 years from registration or start-up of operation, unless specific period is otherwise stated.<sup>3</sup>

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<sup>1</sup> Executive Order No. 226 (1987).

<sup>2</sup> Rep Act No 7042 (1991), as amended by Rep Act No 8179 (1996) hereinafter cited as 'FIA'.

<sup>3</sup> Executive Order No 226 (1987).

Under the FIA, a non-Philippine national not otherwise disqualified by law, may upon mere registration with the Securities and Exchange Commission (SEC) or with the Bureau of Trade and Consumer Protection of the Department of Trade and Industry (DTI), in the case of single proprietorship, do business or invest in a domestic enterprise up to 100% of its capital unless participation of non-Philippine nationals in the enterprise is prohibited or limited to a smaller percentage by law or by the FIA itself.<sup>4</sup> Foreign owned firms catering mainly to the domestic market are encouraged to undertake measures that will gradually increase Filipino participation in their business, implementing the transfer of technology to Filipinos and generating employment.<sup>5</sup>

The term Philippine national means a citizen of the Philippines; or a domestic partnership or association wholly owned by citizens of the Philippines; or a corporation organized under the laws of the Philippines which at least sixty percent (60%) of the capital stock outstanding and entitled to vote is owned and held by citizens of the Philippines; or a corporation organized abroad and registered as doing business in the Philippines under the Corporation Code of which one hundred percent (100%) of the capital stock outstanding and entitled to vote is wholly owned by Filipinos or a trustee of funds for pension or other employee retirement or separation benefits, where the trustee is a Philippine national and at least sixty percent (60%) of the funds will accrue to the benefit of Philippine nationals; *Provided, that* where a corporation and its non-Filipino stockholders own stocks in a Securities and Exchange Commission (SEC) registered enterprise, at least sixty percent (60%) of the capital stock outstanding and entitled to vote of both corporation must be owned and held by citizens of the Philippines and at least sixty percent (60%) of the members of the Board of Directors of both corporations must be citizens of the Philippines, in order that the corporation shall be considered a Philippine national.<sup>6</sup>

The term 'doing business' has been given a technical meaning by law, and generally refers to all 'acts that imply a continuity of commercial dealings or arrangements, and contemplates to that extent the performance of acts or works, or the exercise of some of the functions normally incident to, and in progressive prosecution of, commercial gain or the purpose and object of the business organisations'. It includes soliciting orders, service contracts, opening offices or branches, appointing representatives or distributors domiciled in the Philippines or who in any calendar year stay in the country for periods that total at least 180 days, or participating in the management, supervision or control of any domestic company in the Philippines. However, it does not include the mere investment by a foreign company as a shareholder in a domestic company, the exercise of rights as such shareholder, having a nominee director to represent its interests in

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<sup>4</sup> RL Reyes, ' Foreign Investments in the Philippines', p 1. (Lecture before the UP Institute of Judicial Administration program, 04 October 2003) 26 p Typescript.

<sup>5</sup> Rep Act No 7042 (1991), s 2, para 2.

<sup>6</sup> *Id*, s 3(a).

such corporation nor appointing a representative or distributor domiciled in the Philippines which transacts in its own name and for its own account.<sup>7</sup>

Atty. Rocky Reyes made the following observations on th two laws amending the Omnibus Investments Code:<sup>8</sup>

'The FIA clarified that, as a general rule, export and domestic market enterprises are open to foreign investments to the full extent of their equity. Before the promulgation of the FIA, the Investments Code required prior Board of Investments (BOI) approval before an entity which is not a Philippine national may do business in the Philippines (or for that matter, for any foreign investment in excess of forty percent (40%) of the outstanding enterprise). The FIA removes this requirement and permits non-Philippine nationals not intending to avail of incentives to do business in the Philippines or to invest in up to one hundred percent (100%) of the capital of an export or domestic market enterprise. However, foreign investments are still prohibited in areas reserved to Philippine nationals by the Constitution special laws and the provisions of the FIA.

Republic Act No 8179 broadened the definition of 'Philippine National' to include foreign corporations which are wholly-owned by Filipinos reduced the minimum paid-up capital for domestic market enterprises which can be owned 100% by foreigners to US\$200, 000 removed the Negative List C and the list of strategic enterprises and provided former national-born citizens with certain investment rights'.<sup>9</sup>

Any non-Philippine national may do business or invest in domestic enterprise up to 100% of its capital provided it is investing in domestic market enterprise in areas outside Foreign Investment Negative List (FINL) and brings foreign capital of at least US\$200,000; or it is investing in expert enterprise whose products and services do not fall within Lists A & B of FINL. It is also provided that country or state of applicant must also allow Filipino citizens and corporations to do business therein.

*List of Investment Areas Reserved to Philippine Nationals or Foreign Investment Negative List.*- (a) List A shall consist of areas of activities where foreign equity participation in any domestic or export enterprise engaged in any activity listed therein shall be limited to maximum of 40% as prescribed by Constitution and specific laws; and (b) List B shall consist of areas of activities and enterprises regulated pursuant to law which are defense-related activities, requiring prior clearance and authorization from Department of National Defense or which have implication on public health and morals.

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<sup>7</sup> *Id*, s 3(d).

<sup>8</sup> *R Reyes, op cit*, p 2-3.

<sup>9</sup> *R Reyes, op cit*, p. 2-3.

Republic Act No. 7042 covers all investment areas of economic activities except banking and other financial institutions which are governed and regulated by General Banking Act and other laws under supervision of Central Bank.

Existing enterprises which have been issued certificates of authority to do business or to accept permissible investments under Executive Order No 226, Presidential Decree No 1789 and Republic Act No 5455, whose activities are included in Transitory FINL or in subsequent Negative Lists, are allowed to continue same activities which they have been authorized to do subject to same terms and conditions stipulated in their certificates of registration.

Those whose activities have been previously authorized under Executive Order No 226, Presidential Decree No 1789 and Republic Act No 5455, and whose activities are not in Transitory FINL or in subsequent Negative Lists may opt to be governed by provisions of Act. Said enterprises shall be considered automatically registered with SEC upon surrender of their certificates of authority to BOI. SEC shall issue new certificate of authority upon advise of BOI.

Existing enterprises with more than 40% of foreign equity which have availed of incentives under any of investment incentives laws implemented by BOI may opt to be governed by the Act. In such cases, said enterprises shall be required to surrender their certificates of registration, which shall be deemed express waiver of their privilege to apply for and avail of incentives under incentives law under which they were previously registered. Subject to BOI rules and regulations, said enterprises may be required to refund all capital equipment incentives availed of.

BOI registered enterprises shall be granted following incentives to extent engaged in preferred area of investment: (1) Income tax holiday – full exemption for six years for pioneer firms and four years for non-pioneer firms from date of commercial operation, extendible for another year while registered expanding firms shall be entitled to exemption for income taxes proportionate to their expansion for period of three years from commercial operation; (2) additional deduction from taxable income equal to 50% of labor expenses for five years from registration; (3) tax and duty exemption on imported capital equipment and accompanying spare parts, under certain conditions; (4) tax credit on domestic capital equipment subject to certain conditions; (5) simplification of customs procedures for importation of equipment, spare parts, raw materials and supplies, and exports of processed products; (6) unrestricted use of consigned equipment provides re-export bond is posted unless equipment and spare parts have been imported tax and duty free; (7) employment of foreign nationals in supervisory, technical or advisory positions for five years from registration, extendible for limited periods with certain exceptions; (8) exemption from all taxes and duties on importation of breeding stocks and genetic materials within ten years from date of registration or commercial operation with certain conditions; (9) tax credit on domestic breeding stocks and genetic materials equivalent to 100% provided

purchase is within ten years from date of registration of enterprise; (10) tax credit for taxes and duties on raw material, supplies and semi-manufactured products used in manufacture of export products; (11) access to bonded manufacturing/trading warehouse system of registered export oriented enterprises; (12) exemption from taxes and duties on imported spare parts and required supplies and for consigned equipment; and (13) exemption from wharfage and any export tax, duty, import and fees.<sup>10</sup>

For registered enterprises with operations in less developed areas, the incentives are: (1) automatic entitlement to incentives available to pioneer enterprises regardless of nationality; (2) additional deduction from taxable income equal to 100% of labor expenses for five years from registration; and (3) deduction from taxable income to extent of 100% of cost of necessary and major infrastructure and public facilities constructed.

Export Processing Zone Authority (now PEZA) registered enterprises are also entitled to incentives available to BOI-registered enterprises. Additional incentives are: (1) Merchandise, raw materials, supplies, and other articles brought into export processing zone are exempt from taxes and duties subject to certain conditions; and (2) exemption from local taxes and licenses including real property taxes on production equipment or machineries.

Foreign business entity organized and existing under any laws other than those of Philippines whose purpose is to supervise, superintend, inspect or coordinate its own affiliates, subsidiaries or branches in Asia-Pacific region may be allowed to establish regional or area headquarters in Philippines subject to certain conditions, among which are following: (1) Its activities shall be limited to acting as supervisory, communications and coordinating center for its subsidiaries, affiliates and branches in region and (2) it will not derive any income from sources within Philippines and will not participate in any manner in management of any subsidiary or branch office it might have in Philippines. Regional or area headquarters shall be entitled to following incentives: (1) Exemption from income tax; (2) exemption from contractor's tax; (3) exemption from all kinds of local licenses, fees and duties; (4) tax and duty free importation of training materials; (5) importation of motor vehicles for expatriate executives and their replacement every three years provided taxes and duties are paid upon importation; and (6) exemption from registration requirements. Expatriate executives are entitled to: (1) multiple entry visa, valid for one year including spouses and unmarried children below 21 and exemption from payment of all fees and duties under immigration and alien registration laws; securing alien certificates of registration; and obtaining all types of clearances required by any government department or agency except notice of final departure and tax clearance from Bureau of Internal Revenue; (2) withholding tax of 15% on gross income received; (3) tax and duty free importation of personal and household effects; and (4) travel tax exemption. Foreign company which has established or

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<sup>10</sup> Executive Order No 226 (1987), as amended by Rep Act No 7918 (1995), s 39.

will establish regional or area headquarters may be allowed to establish regional warehouses subject to the following conditions: (1) Its activities shall be limited to serving as supply depot for storage, deposit, safekeeping of its spare parts or manufactured components and raw materials including packing and related activities; filling up transactions and sales made by its head offices or parent companies; and serving as storage or warehouse of goods purchased locally by home office of foreign company for export abroad; (2) it shall not directly engage in trade nor directly solicit business, promote any sale, nor enter into any contract for sale or disposition of goods in the Philippines; and (3) it will not derive any income from sources within the Philippines and its personnel will not participate in any manner in management of subsidiary, affiliate or branch office it might have in the Philippines. Imported spare parts, raw materials and other items for use exclusively on goods stored, brought into regional warehouse from abroad to be kept and re-exported to Asia-Pacific and other foreign markets shall be exempt from payment of customs duty, internal revenue tax, export tax and local taxes.

Special investors resident visa may be issued to any alien who possesses the following qualifications: (1) He has not been convicted of crime involving moral turpitude; (2) he is not afflicted with any loathsome, dangerous or contagious disease; (3) he has not been institutionalized for any mental disorder or disability; and (4) he is willing and able to invest US\$75,000 in the Philippines.

Investors and registered enterprises are entitled to the following basic rights and guarantees:

- (1) repatriation of investment;
- (2) remittance of earnings;
- (3) the right to remit at the exchange rates prevailing at the time of the remittance such sums necessary to meet payments of interest and principal on foreign loans and foreign obligations arising from technological assistance contracts;
- (4) the freedom from expropriation of property represented by investments or property of enterprises except for public use or in the interests of national welfare or defense and, upon payment of just compensation; and
- (5) no requisition of property represented by investment of property of enterprises except for public use or in the interests of national welfare or defense and, upon payment of just compensation; and
- (6) no requisition of property represented by investment of property of enterprises, except in the event of war or national emergency.<sup>11</sup>

With the Special Economic Zone Act of 1995,<sup>12</sup> the government aims to encourage, promote, induce and accelerate sound and balanced industrial, economic and social development in the country by providing jobs in rural areas

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<sup>11</sup> Executive Order No 226 (1987), art 38.

<sup>12</sup> Rep Act No 7916 (1991), as amended by Rep Act No 8748 (1995).

and increasing productivity and income of every individual and family living in these areas through the establishment of special economic zones ('ECOZONES') that will effectively attract legitimate and productive foreign investments.

Special economic zones are selected areas which are highly developed of which have potential to be developed into agro-industrial, industrial, tourist/recreational, commercial, banking, investment and financial centers.

Any investor within economic zone whose initial investment shall not be less than US\$150,000, his/her spouse and dependent children under 21 years old shall be granted permanent resident status within economic zone. Business establishments operating within ECOZONES shall be entitled to: (1) Fiscal incentives under Presidential Decree No 66 or Executive Order No 226; (2) tax credits for exporters using local materials as inputs as provided by Republic Act No 7844 (Export Development Act of 1994); (3) exemption from taxes under National Internal Revenue Code except for real property taxes on land owned by developers; (4) goods manufactured by ECOZONE enterprise shall be made available for immediate domestic retail sales; (5) additional deduction of ½ of value of training expenses incurred by ECOZONE enterprises in developing skilled or unskilled labor or for managerial or other management development programs; and (6) exemption from national and local taxes and licenses.

ECOZONE developers/operators shall be entitled to the following incentives: (1) Exemption from national and local taxes and licenses, and in lieu thereof, ECOZONE developer/operator shall pay 5% final tax on gross income; (2) additional deduction equivalent to ½ of value of training expenses; (3) incentives under BOT law; and (4) other incentives under the Code.

To avail of all above incentives and benefits, business enterprises within ECOZONES must register with the Philippine Economic Zone Authority.

ECOZONE enterprises are allowed to hire foreign nationals in supervisory, technical or advisory capacity not exceeding 5% of its workforce.

Republic Act No 7652 (1993) allows long term leases of private land by foreign investors for the establishment of industrial estates, factories, assembly or processing plants, agro-industrial enterprises, development for industrial or commercial use, tourism, or other similar priority productive endeavors.

Outside the scope of Republic Act No 7042 are the banking and other financial institutions. Republic Act No 8791 otherwise known as the General Banking Law of 2000 regulates the organization and operation of Banks, Quasi-Banks and Trust Entities. The General Banking Law governs primarily universal and commercial banks. Under Section 4 of this Act, Banks are classified into:

- (a) Universal Banks;<sup>13</sup>
- (b) Commercial Banks;
- (c) Thrift Banks, composed of (i) Savings and Mortgage Banks; (ii) Stock Savings and Loan Associations; and (iii) Private Development Banks as defined by Republic Act No 7906 (1995);<sup>14</sup>
- (d) Rural Banks as defined by Republic Act No 7353 (1992);<sup>15</sup>
- (e) Cooperative Banks as defined in Republic Act No 6938 (1990);<sup>16</sup>
- (f) Islamic Banks as defined by Republic Act No 6848 (1990);<sup>17</sup> and
- (g) Other classifications of banks as determined by the Monetary Board of the *Bangko Sentral ng Pilipinas*.<sup>18</sup>

A universal bank, in addition to the powers of a commercial bank, can exercise the powers of an investment house, as well as invest in non-allied enterprises. On the other hand, a commercial bank, apart from its general powers of a stock corporation, can (1) exercise all the powers specified in Section 29; (2) provide other banking services enumerated in Section 53; and (3) purchase, hold and convey real estate as contemplated by Sections 51 and 52 of the General Banking Law. Other laws affecting banks are: the Non-Disclosure Deposits Law;<sup>19</sup> Unclaimed Balances Law,<sup>20</sup> the Philippine Deposit Insurance Corporation Law,<sup>21</sup> and the Foreign Currency Deposit Act.<sup>22</sup>

The General Banking Law and Central Bank<sup>23</sup> Law apply in a supplementary character to all banks wholly owned by the government. By specific provisions of the Central Bank Law, the *Bangko Sentral* is charged with the supervision, regulation, and periodic examination of all the banks operating in the Philippines, including all government banking institutions, such as the Land Bank of the Philippines<sup>24</sup> and the Development Bank of the Philippines.<sup>25</sup>

The supervisory powers of the *Bangko Sentral* shall include the following:

- (1) the issuance of rules of conduct or the establishment of standards of operation for uniform application to all institutions or functions covered, taking into consideration the distinctive character of the operations of institutions and the substantive similarities of specific functions to which such rules, modes or standards are to be applied;

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<sup>13</sup> Concept of Universal Banking was introduced by *Batas Pambansa Blg 61* (1980).

<sup>14</sup> Thrift Banks Act.

<sup>15</sup> Rural Banks Act.

<sup>16</sup> Cooperative Code.

<sup>17</sup> Charter of *Al-Amanah* Islamic Investment Bank of the Philippines.

<sup>18</sup> R A MORALES, *THE PHILIPPINE BANKING LAW (ANNOTATED)* 10 (2004).

<sup>19</sup> Rep Act No 1405 (1955), as amended.

<sup>20</sup> Act No 3936 (1932).

<sup>21</sup> Rep Act No 3591 (1963), as amended.

<sup>22</sup> Rep Act No 6426 (1972), as amended.

<sup>23</sup> Rep Act No 8791 (2000), s 4 in relation to Rep Act No 7653 (1993).

<sup>24</sup> Rep Act No 3844 (1964), as amended, s 97.

<sup>25</sup> Executive Order No 81 (1986), s 21.



- (2) the conduct of examination to determine compliance with the laws and regulations, if the circumstances so warrant as determined by the Monetary Board;
- (3) overseeing to ascertain the laws and regulations are complied with;
- (4) regular investigation which shall not be often than once a year from the last date of examination to determine whether an institution is conducting its business on a safe or sound basis;
- (5) inquiring into the solvency and liquidity of the institutions; or
- (6) enforcing prompting corrective action.<sup>26</sup>

The *Bangko Sentral* shall also have supervision over the operations of and exercise regulatory powers over quasi-banks, trust entities and other financial institutions which under special laws are subject to *Bangko Sentral* supervision.<sup>27</sup>

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<sup>26</sup> Rep Act No 8791 (2000), s 4.

<sup>27</sup> *Id.*