The Legal 500 & The In-House Lawyer
Comparative Legal Guide
Philippines: Mergers & Acquisitions

This country-specific Q&A gives an overview of mergers and acquisition law, the transaction environment and process as well as any special situations that may occur in the Philippines.

It also covers market sectors, regulatory authorities, due diligence, deal protection, public disclosure, governing law, director duties and key influencing factors influencing M&A activity over the next two years.

This Q&A is part of the global guide to Mergers & Acquisitions. For a full list of jurisdictional Mergers & Acquisitions Q&As visit http://www.inhouselawyer.co.uk/index.php/practice-areas/mergers-acquisitions/

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1. **What are the key rules/laws relevant to M&A and who are the key regulatory authorities?**

   M&A activity is governed primarily by the Corporation Code of the Philippines (Batas Pambansa Blg. 68). In M&A transactions where any of the parties is a "public company" (i.e., a corporation with a class of equity securities listed on an exchange, or a corporation with assets in excess of Php50 Million and which has 200 or more holders each holding at least hundred 100 shares of a class of its equity securities), the Securities Regulation Code (Republic Act No. 8799), and its Implementing Rules and Regulations, also becomes relevant (for example, the SRC sets out, among others, reporting obligations for public companies, tender offers, proxy statements and shareholder obligations to disclose ownership and transactions with respect to shares of

public companies). The key regulatory authority is the Securities and Exchange Commission (SEC).

In case of high-value mergers and acquisitions, the Philippine Competition Act (Republic Act No. 10667) and its Implement Rules and Regulations may also become relevant as it provides for a merger control regime in respect of mergers and acquisitions which meet the thresholds provided under the implement rules. The Philippine Competition Commission is the regulatory body tasked with the implementation of this law.

In respect of the tax aspects of M&A activity, the principal law is the Tax Reform for Acceleration and Inclusion (Train) Law (Republic Act No. 10963).

If the M&A involves entities in regulated sectors, there may be special laws applicable to them. For example, in case of banks, the General Banking Law (Republic Act No. 8791) and the New Central Bank Act (Republic Act No. 7653); and in case of insurance companies, the Insurance Code.

2. **What is the current state of the market?**

M&A activity in the Philippines have been robust over the past couple of years.

3. **Which market sectors have been particularly active recently?**

Traditional sectors like power and energy continue to have robust M&A activities. Over the past year, we have seen increased M&A activity in: financial technology, logistics and healthcare industries.

4. **What do you believe will be the three most significant factors influencing M&A activity over the next 2 years?**

First, we believe that the state of the Philippine economy will continue to have a significant influence over the level of M&A activity. Periods of economic upturn has typically been accompanied by an increase in M&A activity, while period of economic downturn (recession, economic or financial crises) see and significant decrease in M&A activity.

Second, there have been proposals to lift the nationality restrictions in certain key industries (e.g., public utilities), with the current President himself expressing support for such proposals. If these proposals come into fruition, we might see increased M&A activity in the pertinent sectors, especially ones involving foreign investors who are currently restricted to holding only a minority stake.

Third, and from a regulatory perspective, we expect the newly-instituted and still-developing merger control regime to continue to have a significant influence in M&A activity. High-value M&A deals now have to comply with a merger notification requirement within 30 days from the signing of the definitive agreements, and closing subject to antitrust clearance being obtained. We have already seen one deal voided for failure to comply with the notification requirement, and several deals having to agree to commitments in order to secure antitrust clearance.

5. **What are the key means of effecting the acquisition of a publicly traded company?**

Acquisitions of publicly traded companies are typically effected through a stock purchase, with the consideration being in cash. Acquisition through a statutory merger is also possible, but this is subject to a higher degree of regulatory control, as mergers have to be approved by the SEC.

6. **What information relating to a target company will be publicly available and to what extent is a target company obliged to disclose diligence related information to a potential acquirer?**

For privately-held companies, their constitute documents and audited financial statements are available to the public and copies thereof may be obtained from the SEC. In addition, they are required to annually file a General Information Sheet with the SEC, which contains information on, among others, the corporation’s directors, officers, shareholders and their shareholdings. The GIS is likewise available to the public.

For public corporations, an even greater amount of information is available to the public. They are required to, among others, file annual and quarterly reports with the SEC and the Philippine Stock Exchange. These reports provide, among others, a description of the company’s business, summaries of material events and transactions, management

discussions and analysis of the results of the company's operations. These companies are also required to immediately disclose material events to the PSE. Copies of these corporation's filings with the PSE are available for viewing and downloading at the PSE's website.

A target company has no general obligation to disclose diligence information to a potential acquirer.

7. To what level of detail is due diligence customarily undertaken?

Acquirers of public or private companies in the Philippines typically conduct due diligence at a high level of detail.

8. What are the key decision-making organs of a target company and what approval rights do shareholders have?

The key decision-making organ is the Board of Directors, which, by provision of law, exercises all corporate powers, conducts all corporate businesses, and controls all corporate properties. Even as the Board can, and typically does, delegate day-to-day management of the corporation to the corporate officers, the Board is expected to supervise the corporate officers in their conduct of corporate officers.

In some instances, the corporation may, through its by-laws, provide for the creation of an executive committee composed of not less than three members of the board, to be appointed by the board. The executive committee may act on such specific matters within the competence of the board, as may be delegated to it in the by-laws or on a majority vote of the board, subject to certain exceptions specified in the Corporation Code.

In respect of shareholder rights, the directors are elected by the shareholders. In terms of approving corporate acts, as general rule, board approval is sufficient to approve corporate acts and shareholder approval is not necessary. However, the ratification or concurrence of shareholders representing at 2/3 of the outstanding capital stock is necessary in respect of extraordinary corporate acts, such as amendment of the articles of incorporation, disposition of all or substantially all of the corporate assets, mergers and consolidations, and liquidation.

9. What are the duties of the directors and controlling shareholders of a target company?

In the Philippines, the fiduciary duties of the members of the board of directors translate to a three-fold duty: duty of obedience, duty of diligence, and duty of loyalty.

Duty of obedience. The directors elected are mandated to perform the duties enjoined on them by law and the by-laws of the corporation. They have the duty to act within the scope of their authority. In this regard, the directors are required to direct the affairs of the corporation only in accordance with the purposes for which it was organized.

Duty of diligence. The directors are required to exercise due care in the performance of their functions. Consequently, they shall be held liable if they willfully and knowingly vote or assent to patently unlawful acts of the corporation, or if they are guilty of gross negligence or bad faith in directing the affairs of the corporation.

Duty of loyalty. Directors owe fiduciary duty to the corporation and to the shareholders. Hence, the directors cannot serve themselves first and their cestuis, second. Because of this duty, the Corporation Code provides for different rules on self-dealing directors (Section 32), contracts between corporations with interlocking directors (Section 30), usurpation of corporate business opportunity (Section 34), and conflict of interest.

In this jurisdiction, controlling shareholders have statutory no duty towards the target corporation.

10. Do employees/other stakeholders have any specific approval, consultation or other rights?

Under Philippine laws, employees or other stakeholders generally have no any specific approval, consultation or other rights.

11. To what degree is conditionality an accepted market feature on acquisitions?

Most M&As contain some degree of conditionality where consummation is subject to the

occurrence or non-occurrence of certain events. M&As which trigger the merger control regime are by law, subject to the condition of antitrust clearance being obtained.

12. What other deal protection and costs coverage mechanisms are most frequently used by acquirers?

Dear protection and cost coverage mechanisms are not very usual in Philippine M&As though we are seeing an increased use of break-up fee provisions, where if the deal does not push through the one responsible for the failure of the deal becomes liable to the other for a specified amount.

13. Which forms of consideration are most commonly used?

The law allows cash and non-cash (e.g., shares of stock, other types of property) to be used as consideration. However, in practice, the most common form of consideration in the Philippines is cash. The use of cash as consideration has practical benefits. For example, for primary subscriptions, if the consideration is non-cash, the consideration must undergo a valuation or appraisal process with the SEC to ensure that the prohibition against issuance of watered stock is not violated.

14. At what ownership levels by an acquirer is public disclosure required (whether acquiring a target company as a whole or a minority stake)?

For public companies, any person who acquires directly or indirectly the beneficial ownership of more than 5% of class of securities of such company is required to make a disclosure with the SEC, the PSE and the company itself, through the submission of a form prescribed by the SEC. Disclosures by the acquirer, through the filing of the prescribed form, are also required where the acquisition will result into ownership in excess of 10%, as well as changes in such 10% ownership.

Both public and private companies, however, are required to submit a GIS, which sets out information on the shareholders and their shareholdings, regardless of ownership percentage.

15. **At what stage of negotiation is public disclosure required or customary?**

For public companies, disclosure is usually done at the signing of the term sheet or at the signing of the definitive agreement. However, in the event that during the course of the negotiations, news or rumors of the potential acquisitions leak into the market, the PSE would typically ask the public company to comment on those reports.

16. **Is there any maximum time period for negotiations or due diligence?**

None.

17. **Are there any circumstances where a minimum price may be set for the shares in a target company?**

If the acquisition will be through a subscription of primary shares, the minimum subscription price will have to be the par value of the shares of stock, since the issuance of watered stock is prohibited by law.

18. **Is it possible for target companies to provide financial assistance?**

There is no general prohibition on the target companies providing financial assistance.

19. **Which governing law is customarily used on acquisitions?**

Under Philippine law, the contracting parties are free to agree and stipulate on the governing law of their contract, subject to certain exceptions, such as that the choice of law must have a substantial connection to the parties or to the transaction. We have thus seen acquisitions agreements governed by foreign laws and by Philippine laws in equal number. However, in respect of agreements relating to the governance of Philippine companies (e.g., shareholders agreements), it has been more usual for such agreements to be governed by Philippine law since, regardless of the governing law of such agreements, corporate governance of Philippine companies remain to be principally governed by Philippine law.

20. What public-facing documentation must a buyer produce in connection with the acquisition of a listed company?

Where a mandatory or compulsory offer is required, the buyer is required to prepare, submit to the SEC, PSE and the company, and publish, a tender offer report which sets out, among others, the terms of the acquisition and the plans of the buyer for the target. Copies of the pertinent agreements between the buyer, the company and the other shareholders are required to be annexed to the tender offer report.

Where the acquired shares will breach the thresholds provided by law, the buyer will have to submit to the SEC, the PSE and the company, reports in the forms prescribed by the SEC, disclosing, among others, the buyer's percentage ownership in the company.

21. What formalities are required in order to document a transfer of shares, including any local transfer taxes or duties?

A simple deed of sale is typically executed to document the transfer, which can be submitted to government authorities where necessary. AT closing, the stock certificates in the name of the seller would have to be cancelled and new ones issued to the buyer. They buyer would also have to be registered as the owner of the acquired shares in the company's stock and transfer book or in the records of the company's stock transfer agent.

Sales of shares trigger documentary stamp taxes and capital gains taxes, unless the shares are listed and are sold in the PSE, in which case, the relevant transfer tax is the stock transaction tax.

22. Are hostile acquisitions a common feature?

Hostile acquisitions are not common in the Philippines.

23. What protections do directors of a target company have against a hostile approach?

As noted in Question No. 23 above, hostile takeovers are not common in the Philippines

and consequently, there is no significant history regarding protections available to directors and the principal shareholders. That said, available defenses can be: (i) white knight defense; (ii) issuance of shares to a friendly third party, etc.

24. Are there circumstances where a buyer may have to make a mandatory or compulsory offer for a target company?

Mandatory or compulsory offers are required only if the target company is a "public company" – i.e., it has a class of equity securities listed on an exchange, or it has assets in excess of Php50 Million and has 200 or more holders each holding at least 100 shares of a class of its equity securities.

A mandatory or compulsory offer is required if: (a) the buyer, alone or with others acting in concert intends to acquire 35% of the outstanding voting shares or such outstanding voting shares that are sufficient to gain control of the board in a public company in one or more transactions within a period of 12 months; (b) the acquisition would result in ownership of over 50% of the total outstanding equity securities of a public company.

25. If an acquirer does not obtain full control of a target company, what rights do minority shareholders enjoy?

Under the Corporation Code, the members of the board of directors are elected among the holders of shares of stocks every year. To ensure representation in the board, minority shareholders may vote by cumulative voting for one candidate, i.e. give one candidate as many votes as the number of directors to be elected multiplied by the number of his shares shall equal. A director elected because of the vote of minority stockholders who united in cumulative voting cannot be removed without cause.

As noted in Question No. 8, the ratification or concurrence of shareholders representing at 2/3 of the outstanding capital stock is necessary in respect of extraordinary corporate acts, such as amendment of the articles of incorporation, disposition of all or substantially all of the corporate assets, mergers and consolidations, and liquidation. Thus, where the minority constitutes at least 2/3 of the corporation's outstanding capital stock, they have a negative veto in respect of such corporate actions.

Minority shareholders also have an appraisal right in certain cases. The appraisal right is the right of a shareholder to demand payment of the fair value of their shares after dissenting from a proposed corporate action involving a fundamental change in the charter or articles of incorporation. The appraisal right exists in the following cases: (a) in case any amendment to the articles of incorporation has the effect of changing or restricting the rights of any stockholder or class of shares, or of authorizing preferences in any respect superior to those of outstanding shares of any class, or of extending or shortening the term of corporate existence; (b) in case of sale, lease, exchange, transfer, mortgage, pledge or other disposition of all or substantially all of the corporate property and assets as provided in the Corporation Code; (c) in case of merger or consolidation; and (d) in case corporation decides to invest its fund in another corporation or business for any purpose other than its primary purposes.

Furthermore, minority shareholders have a right to institute individual suit, representative suit, and derivative suit. Individual suit is available when a wrong is directly inflicted against a shareholder, the latter can maintain an individual or direct suit in his own name against the corporation. Representative suit may be resorted to when a wrong is committed against a group of shareholders, in which case a shareholder may bring a suit in behalf of himself and all other shareholders who are similarly situated. Lastly, an action is derivative, i.e. in the corporate right, if the gravamen of the complaint is injury to the corporation or to the whole body of its stock or property without any severance or distribution among individual holders, or if it seeks to recover assets for the corporation or to prevent the dissipation of its assets.

26. Is a mechanism available to compulsorily acquire minority stakes?

There is none. The Philippines has no squeezed-out mechanisms as they are known in other jurisdictions.