

# 10 QUESTIONS INVESTORS NEED TO ASK BEFORE INVESTING IN THE PHILIPPINES

# 1

## What are the different forms of investment one can use?

This is critical and fundamental because each form has its own characteristics, requirements, advantages and disadvantages that may affect or influence one's decision in determining which form best suits the business to be established or investment to be made.

A **sole proprietorship** is the basic and least complex form of business organization, because it is not saddled with the many requirements and regulations to which corporations are often subjected to by law. It is not endowed with a separate juridical personality, meaning, the owner is in command of his whole business, and in the event that the business venture goes bankrupt, he stands to lose as much as he puts in and even more to the extent of all his personal holdings.

This business form work well for carrying on simple or small business endeavors, and do not function well in cases of large enterprises which require huge capital investments and specialized management skills.

A **partnership** is a business arrangement entered into by two or more persons bind themselves to contribute money, property, or industry to a common fund, with the intention of dividing the profits among themselves. While a partnership has a separate juridical personality, it does not have the right of succession. This means that the partnership will automatically be dissolved in case of death, incapacity, withdrawal or insolvency of any of the partners.

Generally, every partner is an agent of the partnership, and by his sole act, he can bind the partnership. Partners are likewise generally liable personally for partnership debts, not only up to the extent of what they have invested in the partnership, but even as to their other properties.

Foreign nationals may invest as a limited or a general partner.

A **corporation** is an artificial being created by operation of law, having the right of succession and the powers, attributes and properties expressly authorized by law or incident to its existence. Being an artificial being allows a corporation to own properties in its own name and its properties are not the properties of any of its stockholders, directors or officers. Unlike a partnership, it has the right of succession, which enables it to have continuity of existence despite the changes on the persons who compose it. Free transferability of the units of ownership, in the form of stocks and evidenced by stock certificates, is a hallmark feature in the corporate setting.

Foreign entities or nationals are allowed, within the limits allowed by law, to establish and/or invest in a domestic corporation, whether such corporation is a new entity, a subsidiary, or a branch.

A branch is merely an extension of the head office, which can be set up with only one (1) person who will act as the resident agent of the said branch. Generally, as a 100% foreign-owned entity, a branch must have a capital of at least USD 200,000. Being a mere extension, a branch's liabilities are considered liabilities of the head office.

For its part, a subsidiary is a corporation incorporated and existing under Philippine laws, therefore domestic; but is also considered foreign because it is wholly or majority owned by a foreign or a parent corporation. It is a juridical entity separate and distinct from that of its parent company, and thus follows the Philippine incorporation requirements of, among others, having at least five (5) but not more than fifteen (15) directors/incorporators, majority of whom must be residents of the Philippines. Being a separate and independent entity, its liabilities are generally not regarded as the liabilities of the parent company. A subsidiary with more than 40% foreign equity must also have a minimum paid up capital of at least USD 200,000 unless the company will be exporting goods or services or generating revenue from abroad amounting to more than 60% of its gross sales it can be fully foreign owned, as it is considered an Export Enterprise under the Foreign Investments Act.

Other types of corporate vehicles are as follows:

A Regional or Area Headquarters (RAHQ) acts as an administrative branch of a multinational company. It principally serves as a supervision, communication and coordination center for the multinational's subsidiaries, branches or affiliates in the Asia-Pacific region and other foreign markets. Because of the nature of the presence of such RAHQ in the Philippines, it is not subject to Philippine income tax and it enjoys certain other incentives under the Omnibus Investment Code and the National Internal Revenue Code (NIRC).

A Regional Operating Headquarters (ROHQ) is a multinational company's branch in the Philippines which is allowed to derive income solely by providing qualifying services<sup>1</sup> to the multinational company's own affiliates, subsidiaries, and branches in the Philippines, in the Asia Pacific Region, and other foreign markets as declared in the its registration with the Securities and Exchange Commission. With very defined qualifying services, a ROHQ is not allowed to perform general business activities in the Philippines, and it can only offer such services to the markets mentioned above. Its income is subject to a preferential income tax rate of ten percent (10%) on taxable income and enjoys certain other incentives under the Omnibus Investment Code.

A Representative or Liaison Office may also be established to deal directly with the clients of its parent company. It acts as a message center between its head office and the Philippine clients, while at the same time promoting the products and services of the head office and its affiliates. As these services are non-income producing, all its expenses are fully subsidized by its head office. From a tax perspective, the only income of this type of corporate vehicle is passive income, such as interest on deposits.

A Regional Warehouse is established by a multinational foreign company simultaneously with or subsequently after the establishment of a ROHQ or a RAHQ. A license therefor must be procured from the Philippines Economic Zone Authority (PEZA) or from the appropriate economic zone authorities, if it will be located in Special Economic Zones. Its activities are limited to serving as a supply depot for the storage, deposit, and safekeeping of its products and materials; filling up transaction and sales made by its head office or parent company; and serving as a storage or warehouse of goods purchased locally by its home office for export abroad. It is not allowed to engage in trade or business nor enter into contracts for the sale and disposition of goods in the Philippines.

A foreign corporation has the right to transact business in the Philippines after it has obtained the necessary license. Without such license, it would not have the right to maintain any action or proceeding before Philippine courts, but may be sued or proceeded against on any valid cause of action recognized by Philippine laws.

Foreign corporations are bound by all laws, rules, and regulations applicable to domestic corporations of the same class. Nonresident foreign corporations, for their part, are generally taxed in a different manner. However, the laws of the place of incorporation will continue to govern the creation, formation, organization, or dissolution of foreign corporations; and fix the relations, liabilities, responsibilities, or duties of stockholders, members, or officers of corporations to each other or to the corporation.

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<sup>1</sup> The qualifying services are the following: general administration and planning, business planning and coordination, sourcing or procurement of raw materials and components, corporate finance advisory services, marketing control and sales promotion, training and personnel management, logistics services, research and development services, product development, technical support and maintenance, data processing and communication and business development.

# 2

## Are there foreign ownership limits in my industry?

The law governing foreign participation in economic and commercial activities in the Philippines is the Foreign Investments Act, which has been liberalized to facilitate entry of foreign investments. Foreigners may own or hold interests in entities engaged in all areas of investment, except in activities reserved by law to Filipino citizens. The Tenth Regular Foreign Investment Negative List, issued last 29 May 2015, is the last released list and it enumerates the areas of investment wherein foreign equity is either prohibited or limited.

List A includes areas reserved to Filipinos as mandated by the Constitution and special laws, and List B includes those investments that are related to defense and security, public health and morals, small and medium-scale enterprises, among others.

### LIST A No Foreign Equity

- Mass media, except recording<sup>2</sup>
- Practice of the following professions<sup>3</sup>:
  - Pharmacy<sup>4</sup>
  - Radiologic and x-ray technology<sup>5</sup>
  - Criminology<sup>6</sup>
  - Forestry<sup>7</sup>
  - Law<sup>8</sup>
- Retail trade enterprises with paid-up capital of less than USDD 2.5 Million<sup>9</sup>
- Cooperatives<sup>10</sup>
- Private security agencies<sup>11</sup>
- Small-scale mining<sup>12</sup>
- Utilization of marine resources in archipelagic waters, territorial sea, and exclusive economic zone as well as small-scale utilization of natural resources in rivers, lakes, bays, and lagoons<sup>13</sup>
- Ownership, operation and management of cockpits<sup>14</sup>
- Manufacture, repair, stockpiling and/or distribution of nuclear weapons<sup>15</sup>
- Manufacture of firecrackers and other pyrotechnic devices<sup>16</sup>
- Domestic investments<sup>17</sup>

<sup>2</sup> Article XVI, Section 11 of the Constitution; Presidential Memorandum dated 05 May 1994

<sup>3</sup> Article XII, Section 14 of the Constitution, Sec. 1 of R.A. No. 5181, Sec. 7(j) of R.A. No. 8981

<sup>4</sup> R.A. No. 5921

<sup>5</sup> R.A. No. 7431

<sup>6</sup> R.A. 6506

<sup>7</sup> R.A. 6239

<sup>8</sup> Art. VIII, Section 5, Constitution; Rule 138, Section 2 of the Rules of Court of the Philippines

<sup>9</sup> Sec. 5, R.A. No. 8762

<sup>10</sup> Ch. III, Article 26 of R.A. No. 6938

<sup>11</sup> Sec. 4, R.A. No. 5487

<sup>12</sup> Sec. 3, R.A. No. 7076

<sup>13</sup> Art. XII, Sec. 2 of the Constitution

<sup>14</sup> Sec. 5, P.D. No. 449

<sup>15</sup> Art. II, Sec. 8 of the Constitution

<sup>16</sup> Sec. 5, R.A. No. 7183

<sup>17</sup> Art. II, Sec. 8 of the Constitution's Conventions/Treaties to which the Philippines is a signatory

### Up to Twenty Percent (20%) Foreign Equity

- Private radio communications network<sup>18</sup>

### Up to Twenty Five Percent (25%) Foreign Equity

- Private recruitment, whether for local or overseas, employment<sup>19</sup>
- Contracts for the construction and repair of locally-funded public works,<sup>20</sup> except:
  - Infrastructure/Development projects covered by R.A. No. 7718; and
  - Projects which are foreign-funded or –assisted and required to undergo international competitive bidding<sup>21</sup>
- Construction of defense-related structures<sup>22</sup>

### Up to Forty Percent (40%) Foreign Equity

- Exploration, development and utilization of natural resources<sup>23</sup>
- Ownership of private lands<sup>24</sup>
- Operation of public utilities<sup>25</sup>
- Culture, production, milling, processing, trading except retail of rice and corn and acquiring, by barter, purchase or otherwise, rice and corn and the by-products thereof<sup>26</sup>
- Contracts for the supply of materials, goods and commodities to government-owned or –controlled corporation, company, agency or municipal corporation<sup>27</sup>
- Facility operator of an infrastructure or a development facility requiring a public utility franchise<sup>28</sup>
- Operation of deep sea commercial fishing vessels<sup>29</sup>
- Adjustment companies<sup>30</sup>
- Ownership of condominium units<sup>31</sup>

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<sup>18</sup> R.A. No. 3846

<sup>19</sup> Art. 27, P.D. No. 442

<sup>20</sup> Sec 1, Commonwealth Act No. 541; Letter of Instruction No. 630

<sup>21</sup> Sec. 2(a), R.A. No. 7718

<sup>22</sup> Sec. 1, C.A. 541

<sup>23</sup> Art. XII, Sec. 2 of the Constitution

<sup>24</sup> Art. VII, Sec. 7 of the Constitution; Ch. 5, Sec. 22, C.A. 141; Sec. 4, R.A. No. 9182

<sup>25</sup> Art. XII, Sec. 11 of the Constitution; Sec. 16, C.A. 146

<sup>26</sup> Sec. 5, P.D. No. 194

<sup>27</sup> Sec. 1, R.A. No. 5183

<sup>28</sup> Art. XII, Sec. 11 of the Constitution; Sec. 2(a), R.A. No. 7718)

<sup>29</sup> Sec. 27, R.A. No. 8550

<sup>30</sup> Sec. 323, P.D. No. 612

<sup>31</sup> Sec. 5, R.A. No. 4726

Up to Forty Nine Percent (49%) Foreign Equity

- Lending companies regulated by the SEC<sup>32</sup>

Up to Sixty Percent (60%) Foreign Equity

- Financing companies and investment houses regulated by the SEC<sup>33</sup>

LIST B

Up to Forty Percent (40%) Foreign Equity

- Manufacture, repair, storage, and/or distribution of products and/or ingredients requiring Philippine National Police (PNP) clearance
- Manufacture, repair, storage, and/or distribution of products and/or ingredients requiring Department of National Defense (DND) clearance
- Manufacture and distribution of dangerous drugs<sup>34</sup>
- Sauna and steam bathhouses, massage clinics and other like activities regulated by law because of risks posed to public health and morals<sup>35</sup>
- All forms of gambling,<sup>36</sup> except those covered by investment agreements with PAGCOR<sup>37</sup>
- Domestic market enterprises with paid-in capital of less than the equivalent of USD 200,000<sup>38</sup>
- Domestic market enterprises which involve advanced technology or employ at least fifty (50) direct employees with paid-in equity capital of less than the equivalent of USD 100,000<sup>39</sup>

# 3

## What government agencies are involved in making an investment in the Philippines?

The three (3) main national government agencies involved in investment are the:

1. Securities and Exchange Commission (SEC);
2. Department of Trade and Industry (DTI); and
3. Bureau of Internal Revenue (BIR);

<sup>32</sup> Sec. 6, R.A. No. 9474

<sup>33</sup> Sec. 6, R.A. No. 5980, as amended by R.A. No. 8556; P.D. No. 129, as amended by R.A. No. 8366

<sup>34</sup> R.A. No. 7042, as amended by R.A. No. 8179

<sup>35</sup> R.A. No. 7042, as amended by R.A. No. 8179

<sup>36</sup> R.A. No. 7042, as amended by R.A. No. 8179

<sup>37</sup> P.D. No. 1869, as amended by R.A. No. 9487

<sup>38</sup> R.A. No. 7042, as amended by R.A. No. 8179

<sup>39</sup> R.A. No. 7042, as amended by R.A. No. 8179

Principally, the SEC is the government agency responsible for the registration, licensing, regulation and supervision of all corporations and partnerships organized in the Philippines, including foreign corporations licensed to engage in business or to establish branch offices in the Philippines. For taxation purposes, any person, whether natural or juridical, is required under the authority of the NIRC to register with the BIR, to enable it to make, render, or file a return, statement or other documents, after having been correspondingly supplied with a Tax Identification Number (TIN). Registration with the SEC and the BIR grants the business entity to operate and engage in business.

While the SEC deals with partnerships and corporations, registration with DTI is required in order to establish a sole proprietorship. It is in this agency where the business name must be registered to allow the business owner to use, sign, and exhibit in plain view the business name.

Usually, the next step is to deal with the local government units (LGUs), namely, the Barangay and the Mayor's Office, to obtain the Barangay Clearance and Business Permit respectively, without which one cannot move forward with the establishment of his business in the owner's chosen location. The certificate of registration from the SEC (or from DTI, in case of sole proprietorship), the Barangay Clearance and Mayor's Business Permit are all required to be allowed registration in the BIR.

There are other government agencies whose approvals may be required depending on the nature of the business and the kind of incentives that one intends to avail of. These are: Board of Investments (BOI), Philippine Economic Zone Authority (PEZA), Subic Bay Metropolitan Authority (SBMA), Clark Development Corporation (CDC), among others. The government agency where application is to be submitted generally depends on the location of the project or activity.

## 4

### **Are there any restrictions when remitting dividends or branch profits abroad?**

Dividend and profit remittances as well as capital repatriation are generally not regulated. All investors and registered enterprises are entitled to the basic rights and guarantees provided in the Constitution. Among the rights recognized by the Philippine government is the right to remit earnings from the investment, in the currency in which the investment was originally made and at the exchange rate prevailing at the time of remittance, subject to the provisions of Section 74 of R.A. No. 265, as amended.

Foreign investments registered with the Bangko Sentral ng Pilipinas (BSP) may repatriate capital and remit dividends, profit, and earnings, using foreign exchange sourced from the domestic banking system. Without registration, remittances using foreign exchange may only be sourced outside the domestic banking system.

## 5

### **What is the extent of participation granted to foreigners in running the company?**

The Philippines allows foreigners to have full participation in an investment, provided the activity or business to be engaged in is not reserved by law to Filipinos, and subject to conditions provided by law.

The Corporation Code states that powers of the corporation are to be exercised by the Board of Directors. It is also provided therein foreigners may be incorporators or directors, subject only to the condition that: (a) a majority of the directors reside in the Philippines; and (b) that they own at least one (1) share of stock in the company. The Corporate Secretary, however, must be a citizen and resident of the Philippines.

Given the discussion on the restrictions placed on foreigners who form part of a company's Board of Directors, it is safe to say that foreign nationals may run the whole corporation, so long as the operations of the business activity the corporation is engaged in is not reserved by law to Filipino citizens.

In instances where foreign equity is restricted, such as in the operation of a public utility wherein the law allows foreign equity of up to forty percent (40%), the participation of foreign investors in the entity shall be limited to their proportionate share in its capital. This means that if there are ten (10) seats on the Board of Directors, foreigners may only hold a maximum of four (4) seats. In such instances also wherein the industry is nationalized and the foreign participation is limited, all the executive and managing officers of the entity must be citizens of the Philippines.

# 6

## What are the requirements if I want to hire a foreign national as an employee?

The owner of the entity deciding to hire a foreign national must obtain an Authority to Employ an Alien from the Department of Justice, where the employment is in a nationalized or partially nationalized industry.

The bulk of the requirements lie with the foreign national. Before he can be employed in the Philippines, he must first comply with the requirements of the law. These requirements include the obtainment of a work visa (9g) from the Bureau of Immigration (BI) to legally engage in gainful employment in the country. Such foreign national must likewise obtain the required Special Temporary Permit (STP) from the Professional Regulation Commission (PRC) in case the employment involves practice of profession.

Likewise, the foreign national is required to obtain an Alien Employment Permit (AEP). The issuance of AEPs, however, is subject to the condition that there is no person available in the Philippines who is competent, able, and willing to perform the services for which the foreign national is desired. An AEP must be secured regardless of the source of compensation and duration of employment, or whether it is part time or temporary.

# 7

## What are the rules in hiring and firing employees?

Any investor, whether local or foreign, must adhere to Philippine labor laws. All employers must comply with the minimum terms, conditions, and benefits of employment stated in the Labor Code and other labor-related special laws. These rights include, but are not limited to, hours of work, rest periods, holidays, leaves, wages, working conditions, security of tenure, and termination procedures.

### Employment-At-Will

Employment-at-will is an employment arrangement, widely adopted in the United States, whereby employment is terminable by either the employer or employee for any reason whatsoever. This arrangement works in such a way that when an employee does not have a written employment contract and the term of employment is indefinite, the employer can terminate the employee for good cause, bad cause, or no cause at all. It is important to note that an employment-at-will arrangement is not allowed in the Philippines.



In the Philippines, the employer has the right to hire, discipline and terminate employees. The employees, in turn, have the right to security of tenure. This means that they may be removed only for causes authorized by law, and in the manner provided by law. An employee has the right to question the validity of his dismissal, and the proper Philippine authorities will determine if there was a violation of substantive and/or procedural due process in terminating the employee.

Any termination without cause is considered as illegal dismissal, which would entitle the concerned employee to backwages or reinstatement, or separation pay, depending on the circumstances. The employer must be certain that all the requirements of due process have been complied with before terminating an employment relationship.

# 8

## How do I take back my investment?

Pulling out of investment in the Philippines takes many forms. One such form is the dissolution of the entity or corporation established in the country with the intent to fully discontinue its operations.

**Dissolution** in the Philippines is the stage of terminating the life of a corporation. If the corporate vehicle used is a business organization organized under Philippine laws, then the dissolution of such business entity must also adhere to requirements provided by the same laws.

For its part, a foreign corporation licensed to do business in the Philippines may cease doing business in the country by filing a petition for withdrawal, which will only be granted after compliance with certain requirements, such as but not limited to, the settlement of all Philippine-accrued claims and the payment all taxes due.

### Repatriation of Capital

Repatriation of capital depends on whether the investment is duly registered with the BSP or not.

According to current rules, only foreign direct investments registered with the BSP, evidenced by the Bangko Sentral Registration Document (BSRD), are entitled to full repatriation of capital using foreign exchange (FX) sourced or purchased from authorized agent banks (AABs) and/or their subsidiary/affiliate foreign exchange corporations.

In the case of unregistered foreign investments, capital repatriation is likewise allowed but the same will be serviced using foreign exchange sourced from outside the domestic banking system.

# 9

## What kinds of taxes are imposed?

In general, businesses will be required to pay national and local taxes. The latter is paid to the city or municipality where the person/entity holds business.

Tax	Tax Description
Corporate Income Tax	Domestic corporations are subject to 30% of net income from sources within and without the Philippines.  Foreign corporations are taxed on income derived from sources within the Philippines only. Resident foreign corporations are taxed 30% of net taxable income, and for non-resident foreign corporations, 30% of gross income.
Minimum Corporate Income Tax (MCIT)	MCIT is not an additional tax. The MCIT, which is 2% of the gross income, is compared with the regular income tax, which is due from a corporation. If the regular income is higher than the MCIT, then the corporation does not pay the MCIT but the amount of the regular income tax.
Local Business Tax (LBT)	LBT is due in the city or municipality where the following are located: (1) the principal office; (2) branches or sales offices, provided they perform operations of the business as an extension of the principal office and record the related sales or transactions; and (3) the factory, project office, plant or plantation, in the case of manufacturers, assemblers, contractors, producers, and exporters.
Real Property Tax (RPT)	The tax rate for RPT is 2% of the assessed value of the property.
Value Added Tax (VAT)	This 12% tax on consumption levied on the sale, barter, exchange, or lease of goods or properties and services in, and importation of goods into, the Philippines, which is imposed when the gross sales or receipts in a 12-month period exceed PHP1,919,500.  Percentage tax on certain businesses is allowed as an alternative to VAT.
Documentary Stamp Tax	This is affixed to certain documents, instruments, and papers evidencing certain business transactions. The tax rate is depends on the contract value or is charged on a per-document basis.
Fringe Benefits Tax	This is imposed on the grossed-up monetary value of fringe benefits granted to an employee, except rank and file. But such taxes are not required if the benefit is necessary for or required by the nature of the business, or if such benefit is to the advantage of the employer.
Dividends Tax	Dividends declared are generally taxed at 30%, reduced to 15% if the home country of the foreign corporation allows a credit against the tax due from the foreign corporation deemed paid in the Philippines equivalent to 15%.
Branch Profits	Profits remitted to a foreign corporation by a branch are taxed at 15%, unless registered with PEZA or other free port zones.
Excise Tax	This is levied on goods manufactured or produced in the Philippines for domestic sale or consumption or for any other disposition, and on things imported.

This is not a comprehensive discussion on the subject but is intended only to answer the commonly asked questions by those interested in doing business in the Philippines. Should specific problems arise, it is still best to refer to the laws of the Philippines as well as obtain more precise legal advice. This guide contains only concise discussions with reference to prevailing rules and laws as of September 2016.

# 10

## What are the incentive privileges that may be enjoyed by Board of Investment (BOI)-registered enterprises?

A foreign corporation may opt to register with the Board of Investment (BOI) in order to avail of the tax breaks and other incentives given to BOI-registered entities that engage in activities identified as investment priorities. At this time, the investment priority areas are: (1) Business Process Outsourcing; (2) Electronics Industry; (3) Renewable Energy; and (4) Shipbuilding.

The following are the incentives available to BOI-registered enterprises:

(a) Fiscal Incentives

- Income Tax Holiday (ITH)
- Exemption from taxes and duties on imported spare parts (NOLCO)
- Exemption from wharfage dues and export tax, duty, impost and fees (GIE)
- Reduction of the Rates of Duty on Capital Equipment, Spare parts and Accessories by Virtue of EO 528
- Tax exemption on breeding stocks and genetic materials
- Tax Credits
- Additional deductions from Taxable Income

(b) Non-Fiscal Incentives

- Employment of Foreign Nationals
- Simplification of customs procedures
- Importation of consigned equipment
- Privilege to operate a bonded manufacturing/trading warehouse



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