

Philippines

Corporate Governance Institutions, Practices and Developments

1. Key Institutional Features of Corporate Governance and Company Profile in the Philippines

1.1 Background

There are four external influences on Philippine Corporate Governance

- The legal system
- The regulatory system
- The judicial system
- Financial reporting standards

The legal system as an external influence includes such laws as the Corporation Code, the Securities Regulation Code (SRC), the General Banking Act and the New Central Bank Act. The regulatory system encompasses rules and regulations issued by agencies that regulate corporate entities [Securities and Exchange Commission (SEC)]; publicly listed firms [SEC/Philippine Stock Exchange (PSE)] and financial institutions [SEC/Bangko Sentral ng Pilipinas (BSP)]. These rules and regulations have influenced corporate governance reforms.

Under Republic Act (R.A.) 7653 (New Central Bank Act, 10 June 1993), the BSP shall have supervision over the operations of banks and exercise such regulatory powers as provided in the law. On 12 April 2000 R.A. 8791 (General Banking Act) was passed into law to regulate the organization and operations of banks, quasi-banks and trust entities. Some of its provisions related to corporate governance are as follows:

- Restriction on bank exposure of directors, officers, stockholders and their related interests (DOSRI);
- Review by the Monetary Board of the qualifications and disqualifications of Individuals elected or appointed bank directors and officers;
- Prescribe at least five and maximum of 15 directors, two of whom shall be independent directors; and
- Disclosure of transactions with the bank by family groups and related interests.

The PSE provides the market for the trading of securities. In June 1998, the SEC granted PSE a Self-Regulatory Organization status, authorizing it to impose rules and penalties on erring trading participants and listed companies.

The SRC was enacted into law on 8 August 2000. One of the objectives of the SRC is to encourage the widest participation of ownership in enterprises. The SRC incorporates and modified certain provisions of the Revised Securities Act of 1982 and the earlier Securities Act of 1937. The SRC was patterned after the 1933 US Securities Act and the 1934 US Securities

Exchange Act. For the protection of investors, SRC requires the filing of annual reports and periodic reports necessary to update investors on its business operation.

Under R.A. 799 or the SRC, the Philippine judiciary is now vested with original jurisdiction to hear cases that were used to be resolved by the SEC. Decisions of the Regional Trial Courts are appealable to the Court of Appeals (CA) and all cases decided by the CA can be brought to the Supreme Court for final review. The following are cases covered by the Philippine judiciary:

- Devices or schemes employed by or any acts, of the board of directors, business associates, its officers or partnership, amounting to fraud and misrepresentation which may be detrimental to the interest of the public and/or of the stockholder, partners, members of associations or organizations registered with the Commission;
- Controversies arising out of intra-corporate or partnership relations, between and among stockholders, members, or associates; between any or all of them and the corporation, partnership or association of which they are stockholders, members or associates, respectively; and between such corporation, partnership or association and the state insofar as it concerns their individual franchise or right to exist as such entity; and
- Controversies in the election or appointments of directors, trustees, officers or managers of such corporations, partnerships or associations.
- Claims for profits on transactions of directors, officers and principal stockholders who own more than 10% of any class or equity realized from unfair use of information obtained as owner/director within any period of less than six months.

Financial Reporting Standards are set by the Generally Accepted Accounting Principles (GAAP). According to SRC Rule 68, GAAP represents accounting principles that are promulgated by the following:

- SEC
- Financial Reporting Standards Council
- Standards issued by the International Financial Reporting Standards Board
- Accounting Principles and Practices

1.2 Trends

	2005	2006	2007	2008	2009
No. of Listed Companies (Year end)	236	239	244	246	248
Market Capitalization* (billion pesos)	5,948.74	7,173.19	7,977.61	4,069.23	6,029.08

Source: PSE Annual Report for 2009

The number of listed domestic companies rose from 234 in 2005 to 246 in 2009. The market capitalization of domestic firms reached P3.99 trillion in 2009, 61.35% higher than its 2008 level. However, this was still lower than the P4.27 trillion recorded in 2007. Total market capitalization including those of foreign corporations rose by 48.16% compared to its 2008 level. The financial sector had the biggest share of market capitalization in 2009 accounting for 43.2% of the aggregate value.

1.3 Key Corporate Governance Rules and Practices

See Key Corporate Governance Rules and Practices in the Philippines, p. 182.

2. Development, Enforcement and Assessment of Implementation of Corporate Governance Rules

2.1 Development of Corporate Governance Rules

The SEC, BSP and the Insurance Commission (IC) are the principal regulatory agencies that promote corporate governance rules in the Philippines. In the private sector, institutions like the PSE and the Institute of Corporate Directors (ICD) play significant roles.

Pursuant to its mandate under the SRC and in accordance with the State's policy to actively promote corporate governance reforms designed to raise investor confidence, develop capital market and help achieve high sustained growth for the corporate sector and the economy, the SEC, in its Resolution No.135, Series of 2002 dated 4 April 2002, approved the promulgation and implementation of the Code of Corporate Governance, which shall be applicable to corporations whose securities are registered or listed, corporations which are grantees of permits/licenses and secondary franchise from the Commission and public companies. This Code also applies to branches or subsidiaries of foreign corporations operating in the Philippines whose securities are registered or listed. The Commission, in its meeting on 18 June 2009, subsequently revised the Code which became effective on 15 July 2009.

2.2 Enforcement of Corporate Governance Rules

The implementation of good corporate governance in the Philippines is the responsibility of three agencies: (a) BSP for the banking sector; (b) SEC for the non-bank financial institutions; and IC for the insurance companies. Each of these three regulators has issued rules for its covered entities. In case of non-compliance, the regulators can impose sanctions that include monetary penalties or revocation of registration.

In line with the program to promote good corporate governance, and towards a fair and efficient market, the PSE continues to enforce the Disclosure Rules among the listed companies. At the same time, the PSE strengthened its campaign to inform the listed companies about the proper observance of Disclosure Rules. In 2008, the total number of violations penalized for non-compliance of structured reportorial requirements increased by 11.3% compared to its 2007 level. However, the total number of cases penalized for non-compliance of unstructured reportorial requirements penalized decreased by 9.6% from its level in 2007.

Summary of Violations and Penalties

Violations	No. of Cases	Amount in P million
Structured		
Annual	30	2.142
Quarterly	29	1.274
Unstructured	47	2,613
Total	106	6.029

Source: PSE Annual Report for 2008

The PSE is in the process of revisiting the revised Disclosure Rules, with the proposed revisions targeted to be elevated to the SEC in 2010.

2.3 Assessment of Corporate Governance Practices

The World Bank Report on the Observance of Standards and Codes [World Bank: 2007] shows that in 2006, the Philippines was partially observing the standards and codes in most corporate governance categories. The table below summarizes this assessment:

CG Category	Finding	Manifestations
Equitable treatment of shareholders	Partially observed	Shareholders have a facility for seeking redress; insider trading is regulated
Disclosure and transparency	Partially observed	Board and management are compliant with disclosure requirements; most of the standards in accounting and auditing are consistent with international standards
Rights of shareholders	Largely observed	Basic shareholders' rights are largely observed; shareholders participate in annual general membership meetings and are allowed to consult with management usually through the Corporate Secretary
Role of shareholders	Partially observed	Stakeholders' legal rights are largely observed while both stakeholder redress and disclosure are partially observed; weak in whistleblower protection and creditors' rights, law and enforcement
Board responsibility	Partially observed	Procedures and mechanisms are partially observed

3. Awareness and Advocacy for Good Corporate Governance

3.1 Company Directors

The Philippine ICD is a non-stock, not-for-profit organization working in close partnership with other business, government, and civil society organizations to promote and uphold the practice of good corporate governance among Philippine Corporations such as publicly-listed companies (PLCs), universal and commercial banks, state-owned enterprise or the Government Owned and Controlled Corporations (GOCCs) and Family-owned corporations (FOCCs).

The ICD is made up mainly of individual corporate directors and reputational agents committed to the professional practice of corporate directorship in the Philippines in line with global principles of modern corporate governance. ICD is working closely with the Organisation for Economic Cooperation and Development (OECD), the Global Corporate Governance Forum, and the International Corporate Governance Network on improving actual boardroom practices: moving away from principles into actual practices.

The ICD is a professional organization of, for, and by corporate directors and other reputational agents for corporate governance. Its mission is

- To attend to the professional needs of corporate directors directly related to their serving on a board of directors.
- To raise the standards for the professional practice of corporate directorship, and to work with partners in a joint pursuit of systemic corporate governance reforms in the Philippines and the East Asian region.
- To accredit corporate directors committed to enhancing the long-term value of the corporation they serve through the observance of corporate governance principles, ethics and social responsibility.

The regulatory bodies: the SEC, the BSP and the IC require that a director must undergo the Corporate Governance Training Program before he/she will be qualified to sit on the board. The ICD and other educational institutions accredited by the regulators offer such training.

Continuing corporate governance education is optional. The ICD offers a professional directorship program and an advanced corporate governance training program in which directors can become ICD Fellows and as such become part of the body that promotes good corporate governance among Philippine corporations. ICD Fellows meet every month at a breakfast roundtable to discuss current issues on corporate governance, providing additional continuing education for participants.

3.2 Media

The PSE and the ICD conducts/sponsors lectures for the media on Corporate Governance. There are no regular reports on corporate governance issues. Reporting is dependent on the personalities involved or the actual issues.

Educational System

The Commission on Higher Education (CHED) is revising the curriculum of some tertiary courses (e.g., Business Administration, etc.) to include subjects on corporate governance and corporate social responsibility. The CHED is the governing body covering both public and private higher education institutions as well as degree-granting programs in all tertiary educational institutions in the Philippines. Established through Republic Act 7722 or the Higher Education Act of 1994, CHED is mandated, among other things, to promote quality education, and ensure the advancement of learning and research, the development of responsible and effective leadership, and the education of capable professionals.

Corporate Governance and Corporate Social Responsibility is a core subject in the MBA program.

3.4 The Stock Exchange

The PSE has programs in support of good governance. One is the conduct of the annual scorecard survey among listed companies, in cooperation with the SEC and the ICD. This serves as a tool for market participants and investors to evaluate the companies' governance practices.

4. Corporate Governance of State-Owned and Family-Controlled Enterprises

4.1 State-Owned Enterprises

The Department of Justice through the Office of the Government Corporate Counsel is the governing authority for government corporations.

Most government corporations have their own supervisory agency as stated in their respective charters. These "mother" agencies may prescribe the adoption of good governance rules. The SEC has issued a general code of corporate governance which may serve as a model for corporations when they register with the SEC.

In 2006, five GOCCs, viz, Development Bank of the Philippines, Philippine Deposit and Insurance Corporation, Philippine Export-Import Credit Agency, Landbank of the Philippines, and the National Transmission Corporation got the highest scores among 31 GOCCs in the Corporate Governance Scorecard (CGS) conducted by the ICD. The conduct of the CGS was in recognition of the sentiments expressed by many sectors in the economy that GOCCs and Government Financial Institutions (GFIs) should help set the tone for improved governance practices. The scorecard created by ICD for GOCCs and GFIs is in accordance with the OECD

Guidelines on Corporate Governance of State-owned Enterprises (SOEs). Five major concerns of corporate governance in SOEs are covered such as ensuring an effective legal and regulatory framework for SOEs, the State acting as an Owner, relations with stakeholders, transparency and disclosure, and the responsibilities of the boards of SOEs.

4.2 Family-Controlled Enterprises

Studies show that the ownership structure in the Philippines is dominated by a few families and individuals. The general public is not a significant investor in the stock market. Family controlled corporations or close corporations must follow the SEC rules on corporate governance. There is no empirical basis to say that family owned corporations consider corporate governance requirements as a disincentive to public listing. Recent research study showed that corporate governance positively influences the financial performance of listed companies in the Philippines.

5. Role of Professional Service Providers in Corporate Governance

Accounting and Auditing firms

Accounting and audit firms provide the public with an objective, independent opinion about the financial position and performance of the companies. They review financial statements in order to determine whether such statements reflect the true financial position of the company.

Rating agencies

A credit rating agency assigns credit ratings for issuers of debt instruments. A credit rating for an issuer takes into consideration the issuer's, and affects the interest rate applied to the particular security being issued.

The value of such ratings is given much weight by the public and is an important factor in the decision to invest.

Commercial banks

Commercial banks offer a wide range of corporate financial services that address the specific needs of private enterprise. They provide deposit, loan and trading facilities, among others. They remain to be the major source of funding for businesses.

Securities analysts

The reports and recommendations made by securities analyst are often used by traders, mutual fund managers, portfolio managers and investors in their decision making processes.

Law firms

Law firms give advice to market participants (issuer, underwriter, fund manager, investors, etc.) and provide opinion on the legality of the issuance and enforceability of the contract and agreements entered into by the parties.

Corporate governance consultants

Corporate governance consultants promote and uphold the practice of good corporate governance. Like the ICD which is comprised of mainly of individual corporate directors and reputational agents committed to the professional practice of corporate directorship in the Philippines in line with global principles of modern corporate governance.

These CG consultants attend to the professional needs of corporate directors directly related to their serving on a Board of Directors and raise the standards for the professional practice of corporate directorship. They accredit corporate directors committed to enhancing the long-term value of the corporation they serve through the observance of corporate governance principles, ethics and social responsibility.

6. Recent Developments in Corporate Governance

6.1 Corporate Governance Developments

The main elements of recent revisions on the Corporate Governance Code (MC No. 6, Series of 2009), which took effect on 15 July 2009:

- Shifting of the responsibility of implementing the provisions of the revised Code from the Compliance Officer to the Board of Directors of the company;
- Expanding the Board's traditional policymaking role to include providing an independent check on management;
- Revision of the definition on the coverage of Corporate Governance specifically to shareholders;
- Inclusion of the provision for Alternative Dispute Resolution in amicable settlement of differences between corporation and stockholders, corporation and third parties, including regulatory authorities;
- Emphasis on the role of the Audit committee and internal control system;
- Implement policies and procedures to ensure integrity and transparency of related party transactions;
- Requirement for Compliance Officer to have at least the rank of VP, and in his absence the corporate secretary to act as such; and
- Inclusion of a provision relative to the regular review of the Code of Corporate Governance and the requirement of submitting a corporate governance scorecard.

6.2 Enforcement of Corporate Governance Rules

The Revised Code of Corporate Governance provides for administrative sanction (a fine of not more than P200,000 (US\$4,380⁸⁶) for every year of violation.

6.3 Current Issues and Challenges for Corporate Governance

Priorities for Reform

- Encourage further broadening of the ownership of publicly listed companies in the Philippine corporate sector to reduce systemic risks involved in highly concentrated ownership;
- Introduce amendments to the Corporation Code to address gaps and concerns on transparency. Some proposed amendments are the following:
 - Require disclosures of underlying ownership of shares held by nominees and holding companies; and

⁸⁶ Based on average exchange rate for the first five months of 2010, P45.6611:US\$1.

— Require disclosures of material changes in ownership

- Further the regime of corporate governance among publicly-listed companies by advocating the creation of minority shareholder groups.
- Include Independent Directors as additional respondents in future corporate governance scorecard surveys.

Financial Crisis

In the banking sector, reforms that encourage the strengthening of capital positions and broaden avenues for risk management, including consolidated and risk-based supervision, the enhancement of corporate governance and disclosure standards and fostering transparency in reporting will continue to be implemented. These initiatives were instrumental in instilling order and depth in the banking system ahead of the onset of the global financial crisis.

Key Corporate Governance Rules and Practices in the Philippines

Element	Yes	No	Source(s) of Rule	Comments
1. Do shareholders add items to the agenda for shareholders' meetings?	X		SL	
2. Do shareholders ask questions of directors at shareholders' meetings and do they receive answers?	X			
3. Must company transactions with its insiders be on a non-preferential basis?				
4. Is a super majority vote required for major company acts affecting shareholder rights?	X		CL	
COMPOSITION AND ROLE OF BOARDS OF DIRECTORS				
5. Must boards have independent directors? What percentage?	X		SL	At least two or 20% of the BoD
6. Do independent directors have significant influence over (a) internal and external audit and (b) executive compensation?	X X		SL CGC	
7. Do independent directors decide what information the board receives from management?				
8. Are the chairman of the board and chief executive officer different persons in the majority of listed companies?	X		CGC	
9. Are all board members elected annually?	X		SL, CGC	
10. Does the board oversee enforcement of a company code of conduct?	X		CGC	
TRANSPARENCY AND DISCLOSURE OF INFORMATION				
11. Do financial statements comply with IFRS ⁵ ?	X		SL, CGC	
12. Are the identities of the five largest shareholders disclosed?	X		SL, CGC	
3. Is compensation of company executive officers disclosed?	X		SL, CGC	

Element	Yes	No	Source(s) of Rule	Comments
14. Are extraordinary corporate events disclosed?	X		SL, CGC	
15. Are risk factors disclosed in securities offering materials?	X		SL	
16. Are transactions of a company with its insiders disclosed?	X		SL, CGC	

Note: CL – company law; SL – securities law; CGC – corporate governance code; SLR – stock exchange listing requirement, GP – general practice but not obligatory

Sources

Securities and Exchange Commission

2009 and 2008 Annual Reports of the Philippine Stock Exchange

Speech by BSP Gov. Amando Tetangco at the Rural Bankers' Association of the Philippines
2009 National Annual Convention, Manila, 15 May 2009

Corporate Governance Country Assessment: Philippines, May 2006, Report on the Observance
of Standards and Codes (ROSC), World Bank