

Republic of the Philippines
House of Representatives
Quezon City

Thirteenth Congress

First Regular Session

HOUSE BILL NO. 124



Introduced by Representative **JOEY SARTE SALCEDA**

EXPLANATORY NOTE

Republic Act No. 8799, otherwise known as the Securities Regulation Code (SRC) was created enacted into law approximately a year ago. It is a landmark legislation designed, among others, to provide for investor confidence, instill professionalism among the industry participants and thereby promote the development of the capital market. Within the same year, however, we have seen certain effects of this law which instead of promoting a vibrant and healthy capital market, have in fact stifled the development of the same.

Section 19.1 ON MANDATORY TENDER OFFERS

Prior to the SRC, the Revised Securities Act (RSA) did not compel a purchaser to make a tender offer even if he was acquiring control of a public company, if his acquisition was through a privately negotiated purchase. This is still the prevailing law in the United States, after which the RSA was patterned.

However, other jurisdictions (notably the United Kingdom and other countries influenced by it) have imposed mandatory tender offer requirements once an acquisition reaches a certain percentage of the total shares (e.g., 30% in the U.K. and 35% in Hongkong). These mandatory tender offer requirements are imposed to give the minority shareholders the opportunity to sell their shares at the same price as the majority shareholders in cases where there is a change in control of the company.

Perhaps following the lead of the U.K. and other countries, Section 19 of the SRC now imposes a mandatory tender offer requirement when 15% or more of the shares is acquired in a single transaction, or 30% or more is acquired over a period of 12 months. Unfortunately, such thresholds are too low. Even in other countries where the shares of public companies are truly widely held, the thresholds are set at around 30% to 35% since control of a widely held company is likely to change at such levels. It is therefore proposed that the threshold be increased to 35%.

To provide the desired protection to minority shareholders, the law should provide that in the event the bidder acquires at least 35% of a public company through privately negotiated purchases, the bidder will be required to make a tender offer to all the other shareholders for the rest of the outstanding shares of the company. However, this should not prevent a bidder who has not made any

privately negotiated purchases, from making a voluntary tender offer to all shareholders for less than all of the outstanding shares of the company. In such a case, if more shares are offered than what the bidder is bound or willing to take up, the shares offered shall be taken up pro-rata according to the number of shares offered by each offeror.

If not changed, the current thresholds of 15% and 30% under Section 19 of the SRC will unduly restrict investments and acquisitions in public companies, since the burdensome and restrictive requirements of a tender offer will have to be complied with even for relatively small transactions which do not result in change in control. Among others, this will discourage foreign investments because many of these investments, although they do not result in control, are normally of such amounts as will reach the 15% or 30% thresholds. This will adversely affect the development of the capital market, which is an avowed policy of the SRC itself.

Section 28.4 (b) ON MINIMUM CAPITAL REQUIREMENTS

Section 28.4 (b) of the SRC has given the Securities and Exchange Commission (SEC) authority to promulgate such rules and regulations to provide minimum net capital requirements for the operation of brokers and dealers.

It is believed that the relevant self-regulatory organization, the primary regulating authority over its broker and dealer members, should have that authority to prescribe the minimum net capital requirements. This amendatory law goes further by authorizing the relevant self-regulatory organization to impose such other capital adequacy ratios to ensure the financial stability of the brokers and dealers.

Section 30.1 ON BROKER-DIRECTOR PROHIBITION

Section 30.1 of the SRC contains the restrictive broker-director prohibition. This rule is damaging to the capital markets and has a direct effect on the volume of trades and the market's efficiency. The prohibition discourages transparency in transactions in the market. A person who in bad faith engages in insider trading will not likely be caught under this rule, as such a person would likely use an unrelated dummy. Insider trading is best addressed by the provisions on insider trading contained in Section 27 of the SRC and in regulatory tools and methods for detecting insider trading. An acceptable and common international practice is merely to require disclosures of insider transactions. Implementation of the broker-director prohibition is unwieldy, if not impossible, as this would require stockholders, officers and employees of brokers or dealers to disclose their relatives to the fourth degree of consanguinity or affinity and any changes thereto. The rule renders brokers and dealers and their employees, who have relatives holding positions of trust in issuer companies, virtually unemployable or otherwise disqualified from working in the brokerage business. These negative consequences of the broker-director prohibition conflicts with the SRC's own declared policy to promote the development of the capital market, and will result in undue burdens on the brokers and dealers and their stockholders, officers and employees.

It is proposed that Section 30.1 be amended such that instead of a blanket prohibition, a broker or dealer may be allowed to buy or sell securities of an issuer in which such broker or dealer is a stockholder, director or officer, provided such broker or dealer complies with such rules as the relevant self-regulatory organization may prescribe to ensure full disclosure of such transactions.

Section 33.2 (c) ON LIMITATION ON OWNERSHIP OF AN EXCHANGE

Section 33.2 (c) of the SRC provides that if an Exchange is organized as a stock corporation, no person may beneficially own or control, directly or indirectly, more than 5% of the voting rights of the Exchange and no industry or business group may beneficially own or control, directly or indirectly, more than 20% of the voting rights of the Exchange.

These prohibitions are designed to curtail the possibility of a single person, entity or aligned individuals or entities, directly or indirectly, from controlling the Exchange. However, it is believed that the prohibition on industry and business groups is uncalled for. Members of an industry or business group may not necessarily be aligned among themselves in respect of ownership structure or business objectives. Thus, there is no logical reason to unduly restrict the members thereof to freely invest in the voting stock of an Exchange. In any event, each member of such group, whether business or industry, is limited to owning, directly or indirectly, 5% of shares of the Exchange. It is therefore believed that the limitation on business and industry groups is not necessary and should be deleted.

As an alternative, this amendatory law proposes that no person or entity, together with their related parties and affiliates, are prohibited from owning or controlling, directly or indirectly, more than 20% of the voting rights of the Exchange.

Section 33.2 (f) ON REPRESENTATION OF BROKERS IN THE BOARD OF THE EXCHANGE BASED ON VOLUME/VALUE OF TRADE AND PAID-UP CAPITAL

Pursuant to Subsection 33.2 (f) of the SRC, representation of brokers in the Board of the Exchange is mandated to be based on the volume/value of trade and paid-up capital of the respective brokers. This is a departure from the rule prescribed in the Corporation Code, whereby the voting power of a stockholder is based on the number of his shares. It is believed that the more democratic rule is that found in the Corporation Code. It is therefore proposed that Subsection 33.2 (f) be amended to delete the clause which states that the brokers shall proportionately represent the Exchange membership in terms of their volume/value of trade and paid-up capital.

Section 34.1 ON BROKER-DEALER PROHIBITION

Section 34.1 of the SRC provides for the segregation of functions of a broker and a dealer. This is ostensibly designed to preclude any conflict of interest situation between a broker and his clients, and prevent the practice of "front-running". This is a departure from the provisions of the Revised Securities Act, whereby the SEC may segregate the function of a broker-dealer, as it deems appropriate in the public interest or for the protection of investors. Thus, the function of a broker-dealer under the RSA was not absolutely prohibited.

It appears that the broker-dealer prohibition in the SRC is an attempt to adopt the prohibition found in the United States Securities Act of 1934, particularly Section 11 (a) 1 thereof. However, the SRC failed to include all the exemptions from the general prohibition provided in the US law. Of particular importance is that exemption in favor of those member-brokers whose gross revenues are primarily derived from (a) underwriting, (b) selling securities to customers, (c) acting as broker, or (d) any combination of the foregoing, provided such member gives priority to orders from non-members.

Brokers, while acting as dealers, are catalysts to liquidity in the market. They stimulate short-term trading from the public. This provides demand and supply from investors, at moments when long-term investors may not be present in the market in sufficient size. Being at the front of the

market, they are the first to sense the point of equilibrium or balance between supply and demand, the momentum, and the direction or a change of direction in the market. They lead a herd of copycats, as it were. Without dealer intermediation, without a lead to follow, public trading activity thins out. It should be stressed that this function of short-term public trading provides the investor assurance that there will be a market for his shares, and that shares will also be available for accumulation.

The drastic reduction in the volume of transactions in the securities market since the effectivity of the SRC has a direct relation to the broker-dealer prohibition. Unless the broker-dealer prohibition is lifted, the very existence of the stock exchange will be jeopardized.

The broker-dealer prohibition should be lifted, subject to the imposition of safeguards against front-running. In this respect, it should be noted that the PSE's computerized trading system is programmed to preclude any front-running attempts by any broker.

Since there are sufficient safeguards against front-running, including the fully transparent computerized system in the PSE, it is submitted that the broker-dealer prohibition should be lifted because instead of contributing to the development of the capital market, it will surely impede, if not completely stifle, its growth if not its very existence.

Section 35 ON FEES PAYABLE BY EXCHANGES

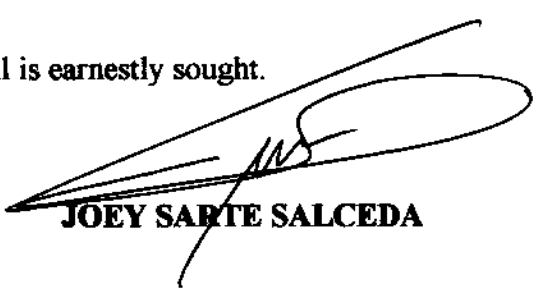
Section 35 of the SRC imposes on an exchange, for the privilege of doing business, a fee of one-hundredth of one per centum (1%) of the aggregate amount of the sales of securities transacted on such exchange.

In view of the regulatory nature of this fee, it is believed that the more reasonable amount of one five-hundredth of one per centum (1%) be imposed. This is necessary to enable exchanges to retain sufficient funds for necessary improvements and changes to keep their systems at par with those of exchanges all over the world.

Section 36.3 ON LISTING IN DIFFERENT EXCHANGES

Securities registered with the SEC and approved for listing in an Exchange should not be deemed automatically listed in other Exchanges. The authority to determine the requirements for listing a particular security in an Exchange should be vested in such Exchange, and not in some other Exchange. This principle should be clarified in the SRC to avoid any doubt or confusion.

From the foregoing, the early passage of this bill is earnestly sought.



JOEY SARTE SALCEDA

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Introduced by **Representative JOEY SARTE SALCEDA**

AN ACT
AMENDING REPUBLIC ACT NO. 8799, OTHERWISE KNOWN AS THE
SECURITIES REGULATION CODE

Be it enacted by the Senate and the House of Representatives of the Philippines in Congress assembled:

SECTION 1. Subsections 19.1 (a) and 19.1 (d) of Republic Act No. 8799, otherwise known as the Securities Regulation Code, are hereby amended to read as follows:

"SEC. 19. *Tender Offers.* –

19.1. (a) Any person or group of persons acting in concert who [intends to] acquireS, **THROUGH PRIVATELY NEGOTIATED PURCHASES**, at least [fifteen percent (15%)] **THIRTY FIVE PERCENT (35%)** of any class of any equity security of a listed corporation or of any class of any equity security of a corporation with assets of at least Fifty Million Pesos (P50,000,000.00) and having two hundred (200) or more stockholders with at least one hundred (100) shares each [or who intends to acquire at least thirty per cent (30%) of such equity over a period of twelve (12) months], shall make a tender offer to **ALL THE OTHER** stockholders **FOR THE REMAINDER OF THE OUTSTANDING EQUITY SECURITIES OF THE CORPORATION IN ACCORDANCE WITH SUCH RULES AS THE COMMISSION MAY PRESCRIBE; PROVIDED, THAT A PERSON OR GROUP OF PERSONS WHO HAVE NOT MADE ANY PRIVATELY NEGOTIATED PURCHASES OF THE EQUITY SECURITIES OF THE CORPORATION MAY MAKE A VOLUNTARY TENDER OFFER FOR LESS THAN ALL OF THE OUTSTANDING EQUITY SECURITIES OF THE CORPORATION IN ACCORDANCE WITH SUCH RULES AS THE COMMISSION MAY PRESCRIBE. THE**

PERSON OR GROUP OF PERSONS MAKING A TENDER OFFER SHALL FILE [by filing] with the Commission a declaration to that effect; [and] furnish the issuer, a statement containing such of the information required in Section 17 of this Code as the Commission may prescribe, [Such person or group of persons shall] **AND** publish all requests or invitations for tender, or materials making a tender offer or requesting or inviting letters of such a security. Copies of any additional material soliciting or requesting such tender offers subsequent to the initial solicitation or request shall contain such information as the Commission may prescribe, and shall be filed with the Commission and sent to the issuer not later than the time copies of such materials are first published or sent or given to security holders.

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d) IN CASES OF VOLUNTARY TENDER OFFERS AND [Where] the securities offered exceed that which a person or group of persons is bound or willing to take up and pay for, the securities that are subject of the tender offer shall be taken up as nearly as may be pro rata, disregarding fractions, according to the number of securities deposited by each depositor. The provisions of this subsection shall also apply to securities deposited within ten (10) days after notice of an increase in the consideration offered to security holders, as described in paragraph (e) of this subsection, is first published or sent or given to security holders."

Section 2. Subsection 28.4 (b) of the same Act is hereby amended to read as follows:

"SEC. 28. *Registration of Brokers, Dealers, Salesmen and Associated Persons.* –

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28.4. x x x x x x

a) x x x x x x

b) In the case of a broker or dealer, the applicant satisfy a minimum net capital **AND OTHER CAPITAL ADEQUACY RATIOS** as prescribed by the **RELEVANT SELF-REGULATORY ORGANIZATION** [Commission], and provide a bond or other security as the **SELF-REGULATORY ORGANIZATION** [Commission] may prescribe to secure compliance with the provisions of this Code; and"

Section 3. Subsection 30.1 of the same Act is hereby amended to read as follows:

"SEC. 30. *Transactions and Responsibility of Brokers and Dealers.* –

30.1. THE RELEVANT SELF-REGULATORY ORGANIZATION SHALL ISSUE THE NECESSARY RULES AND REGULATIONS TO ENSURE FULL DISCLOSURE OF

TRANSACTIONS OF A [No] broker or dealer [shall deal in or otherwise buy or sell, for its own account or for the account of customers,] **IN** securities listed on an Exchange issued by any corporation where any stockholder, director, **OFFICER OR EMPLOYEE OF SUCH BROKER OR DEALER IS ALSO A STOCKHOLDER, DIRECTOR, OFFICER OR EMPLOYEE OF SUCH CORPORATION.** [associated person or salesman, or authorized clerk of said broker or dealer and all the relatives of the foregoing within the fourth civil degree of consanguinity or affinity, is at the time holding office in said issuer corporation as a director, president, vice-president, manager, treasurer, comptroller, secretary or any office of trust and responsibility, or is a controlling person of the issuer.]"

Section 4. Subsections 33.2 (c) and 33.2 (f) of the same Act is hereby amended to read as follows:

"SEC. 33. *Registration of Exchanges.* –

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33.2. x x x x x x

a) x x x x x x

b) x x x x x x

c) Where the Exchange is organized as a stock corporation, that no person may beneficially own or control, directly or indirectly, more than five percent (5%) of the voting rights of the Exchange and no **PERSON, TOGETHER WITH ITS AFFILIATES OR RELATED PARTIES,** [industry or business group] may beneficially own or control, directly or indirectly, more than twenty percent (20%) of the voting rights of the Exchange: Provided, however, That the Commission may adopt rules, regulations or issue an order, upon application, exempting an applicant from this prohibition where it finds that such ownership or control will not negatively impact on the exchange's ability to effectively operate in the public interest.

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f) That the brokers in the board of the Exchange shall comprise of not more than forty-nine percent (49%) of such board [and shall proportionately represent the Exchange membership in terms of volume/value of trade and paid up capital,] and that any natural person associated with a juridical entity that is a member shall himself be deemed to be a member for this purpose: Provided, That any registered Exchange existing prior to the effectivity of this Code shall immediately comply with this requirement;"

Section 5. Section 34.1 of the same Act is hereby repealed, and Sections 34.2 and 34.3 are hereby renumbered as 34.1 and 34.2, respectively.

Section 6. Section 35 of the same Act is hereby amended to read as follows:

"SEC. 35. *Additional Fees of Exchanges.* – In addition to the registration fee prescribed in Section 33 of this Code, every Exchange shall pay to the Commission, on a semestral basis on or before the tenth day of the end of every semester of the calendar year, a fee in such an amount as the Commission shall prescribe, but not more than **ONE FIVE-HUNDREDTH** [one-hundredth] of one per centum (1%) of the aggregate amount of the sales of securities transacted on such Exchange during the preceding calendar year, for the privilege of doing business, during the preceding calendar year or any part thereof."

Section 7. Section 36.3 of the same Act is hereby amended to read as follows.

"SEC. 36. *Powers with Respect to Exchanges and Other Trading Market.* –

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36.3. In addition to the existing Philippine Stock Exchange, the Commission shall have the authority to determine the number, size and location of stock Exchanges, other trading markets and commodity Exchanges and other similar organizations in the light of national or regional requirements for such activities with the view to promote, enhance, protect, conserve or rationalize investment[.]; **PROVIDED, THAT ANY SECURITIES REGISTERED WITH THE COMMISSION AND APPROVED FOR LISTING IN AN EXCHANGE SHALL NOT BE DEEMED AUTOMATICALLY LISTED IN ANY OTHER EXCHANGE.**"

Section 8. This Act shall take effect fifteen (15) days after its complete publication in at least two (2) national papers of general circulation.

Approved,