

Corporate Governance Issues in Philippine-Listed Companies

Arthur S. Cayanan*

University of the Philippines, Cesar E.A. Virata School of Business, Diliman, Quezon City 1101, Philippines

This paper discusses corporate governance issues in Philippine-listed companies such as ownership structure, separation of Chairman and CEO positions, independent directors, related party transactions, among others, and how non-controlling stockholders are adversely affected by these issues. The paper also assesses the sufficiency of existing rules and regulations and the effectiveness of regulators in protecting minority interest.

1 Introduction

Corporate Governance is defined as the system of stewardship and control to guide organizations in fulfilling their long-term economic, moral, legal and social obligations towards their stakeholders.¹

On November 10, 2016, the Securities and Exchange Commission (SEC) approved the Code of Corporate Governance for Publicly-Listed Companies (CG Code for PLCs).² The Code provides a list of the governance responsibilities of the board of directors (BOD), corporate disclosure policies, standards for the selection of external auditor, and duties to stockholders, among others.

In this paper, emphasis will be on ownership structure, the positions of Chairman and Chief Executive Officer (CEO) being held by separate individuals, the independence of independent directors, some related party transactions, and how these issues affect the interest of non-controlling stockholders.³

2 Objectives

This study has the following objectives:

1. To assess some corporate governance practices of the 30 Philippine Stock Exchange index (PSEi) PSEi-indexed stocks, e.g., ownership structure, different individuals holding the positions of the chairman of the BOD and CEO, related party transactions, and tender offers.
2. To raise questions on the effectiveness of the regulatory regime in protecting the interest of the minority stockholders.

3 Review of Literature

La Porta et al. (1999) examined patterns of control in the largest firms from each of 27 wealthy economies. Their data showed that countries with poor investor protection typically exhibit more concentrated control of firms than do countries with good investor protection.

Shleifer and Vishny (1997) concluded that concentrated ownership through large shareholdings and takeovers is a universal method of control that allows these investors to get their money back, which may result in an inefficient distribution of wealth from other investors to themselves. This high ownership concentration creates agency problems between the controlling stockholders and minority stockholders which may result in the expropriation of the latter.

La Porta et al. (2000) identified different forms of expropriation which include the sale of output, assets or additional securities in the companies the large stockholders control to other companies they own at below market prices. La Porta et al. concluded that such transfer pricing, asset stripping and

* Correspondence: Tel: +63 2 928 4571; Fax: +63 2 929 7991. Email: arthur.cayanan@gmail.com

An earlier version of this paper was presented at the UP-BSP Professorial Chair Lectures on November 22, 2018 (Cayanan, 2018).

¹ From Code of Corporate Governance for Publicly-Listed Companies. http://www.sec.gov.ph/wp-content/uploads/2016/12/2016_memo_circular_no.19.pdf

² This Code supersedes SEC Memorandum Circular No. 6, series of 2009 (Revised Code of Corporate Governance).

³ Non-controlling stockholders are also called minority stockholders and external stockholders.

investor dilution, while often legal, are no different from theft. Expropriation may also be in the form of diverting corporate opportunities to their other closely-held corporations, or putting unqualified members of the family in managerial positions and overpaying them for such positions.

Johnson et al. (2000) established a correlation between investor protection and financial crises. They found out that in countries with poor investor protection, the controlling stockholders or insiders might treat minority stockholders well if business prospects are bright and are interested in external financing. When prospects turn sour, the controlling stockholders might step up expropriation, and outside investors, whether minority shareholders or creditors, might be helpless about it. This escalation of expropriation might lead to significant declines in stock prices, especially in countries with poor investor protection.

Claessens et al. (2000) found evidence that concentrated ownership could harm market valuation. Kaplan (1994) explained the adverse effects of keiretsu⁴ affiliation on firms' valuation in Japan, and identified the conflicts of interest between large and small shareholders and economic inefficiencies as possible causes.

In the United States, however, some studies⁵ found a positive correlation between concentrated ownership and corporate valuation. One of the reasons cited was that large shareholders could better monitor management and hence, improve firm valuation. According to these studies, better monitoring and reduced agency costs were associated with concentrated ownership.

Claessens et al. (1999) documented the correlation between cash-flow rights and control rights on market valuation. They concluded that higher cash-flow rights in the hands of block-holders are associated with higher market valuation while concentration of control, particularly for family-held and financial institutions, is associated with lower market valuation. This would be more evident when cash-flow rights are low and control rights are high after adjusting for the level of control.

According to Desender (2009), there are strong perceptions that more independent directors lead to increased good governance as shown in the studies of Fernández-Rodríguez, Gómez-Ansón, and Cuervo-García (2004), and Walsh and Seward (1990).

Bhagat and Black (2002), however, argued that based on their large sample, long-horizon study of American companies, those with more independent directors did not perform better than other companies. Among the reasons cited are the following: ignorance of independent directors on company's operations and lack of incentives to do careful monitoring given their small number of shares in the company. Bhagat and Black also suggested that some directors classified as independent are not really independent. They may be indebted to the companies or to the CEOs in ways that may be hard to capture in the usual definitions of "independence." Some of them maybe advisers or consultants of these companies or are employed by foundations which get donations from these companies where they serve as directors. Pritchard (2009) also stated that in the US, there was no evidence to show that having more independent directors could be associated with better performance.

Jensen (1993) concluded that a small number of directors in the board improves company's performance. According to him, when the number of directors in the board goes beyond seven, these directors become less effective in carrying out their functions and are easier for the CEO to control. Jensen also concluded that having directors with more equity holdings in the company improves corporate governance.

Jensen (1993) explained why the positions of the chairman of the board of directors and CEO should be assigned to different individuals. Among the responsibilities of the chairman are to preside in board meetings and oversee the process of hiring, firing, evaluating, and compensating the CEO. The CEO will have a conflict of interest in carrying out some of these functions if he is also the chairman, especially those affecting his position, performance evaluation and setting his compensation.

Gourevitch (2003) discussed the opposing views on the effects of regulation on securities. A traditional perspective in law and economics suggests that regulation in securities is irrelevant. According to this view, competition in products and capital markets drives companies to come up with rules, including corporate governance mechanisms, that will minimize costs, and make regulation

⁴ A *keiretsu* is a set of companies in Japan with interlocking business relationships and shareholdings.

⁵ These studies include those of Levy, 1983; Lease et al., 1984; DeAngelo and DeAngelo, 1985; Shleifer and Vishny, 1986; McConnell and Servaes, 1990.

useless. Roe's (2019) Quality of Corporate Law (QCL) theory, however, argues that regulation can have positive effects. According to this view, properly structured institutions can come up and enforce rules that can lead to desired objectives, including the protection of external or minority stockholders.

Gourevitch (2003) also discussed the criticism to the QCL theory, the "Capture" model. He cited articles such as that of Noll (1989) who argued that regulation is always captured which suggests that regulated entities always manage to work through politics to make regulators decide in their favor.

Echanis (2006) discussed weaknesses in corporate governance mechanisms in selected Philippine companies and how such weaknesses were partly addressed by regulations and reforms. Her study, however, concluded that such regulations and reforms were not enough due to the following reasons: dominance of one accounting firm, weak enforcement of the laws, concentrated ownership in companies, and weak monitoring system by the regulators.

4 Methodology

In conducting this study, the following activities were made:

1. Reviewed Code of Corporate Governance for publicly listed companies issued by the Securities and Exchange Commission (SEC) in 2016 and which became effective at the start of 2017.
2. Reviewed Corporation Code of the Philippines, especially the provisions which require at least two-third (2/3) votes of the capital stock for a decision to be carried out by a company.
3. Reviewed the 2017 annual reports of the 30 listed Philippine companies which comprise the Philippine stock index (PSEi) where information related to their respective members of the board of directors, top stockholders with voting rights, and the process for nominating directors, including independent directors, were taken from (see Table 1 for the list of the 30 PSEi-indexed stocks and public float⁶ as of October 22, 2018).

Table 1. List of 30 PSEi-indexed Stocks and their Respective Floats as of October 22, 2018

| | Company | Float for Common Stocks as of October 22, 2018 |
|----|--|--|
| 1 | Ayala Corporation (AC) | 43% |
| 2 | Aboitiz Equity Ventures (AEV) | 45% |
| 3 | Alliance Global, Inc. (AGI) | 31% |
| 4 | Ayala Land Inc. (ALI) | 52% |
| 5 | Aboitiz Power Corporation (AP) | 19% |
| 6 | BDO Unibank, Inc. (BDO) | 45% |
| 7 | Bank of the Philippine Islands (BPI) | 48% |
| 8 | DMCI Holdings, Inc. (DMC) | 28% |
| 9 | First Gen Corporation (FGEN) | 32% |
| 10 | Globe Telecom, Inc. (GLO) | 22% |
| 11 | GT Capital Holdings | 44% |
| 12 | International Container Terminal Services, Inc. (ICTS) | 51% |
| 13 | Jollibee Foods Corporation (JFC) | 44% |
| 14 | JG Summit Holdings, Inc. (JGS) | 41% |

⁶ Public float of a company, as defined by SEC, refers to the portion of the issued and outstanding shares that are freely available and tradeable in the market and are non-strategic in nature or those not meant for the purpose of gaining substantial influence on how the company is being managed. Significant shareholdings of 10% or more of the total issued and outstanding shares of the company are considered strategic and thus excluded in the public float of the company (Taken from https://www.sec.gov.ph/wp-content/uploads/2015/10/2017PressRelease_MandatesPublicforIPOs.pdf)

| | Company | Float for Common Stocks as of October 22, 2018 |
|----|---|---|
| 15 | LT Group, Inc. (LTG) | 26% |
| 16 | Metropolitan Bank and Trust Company (MBT) | 49% |
| 17 | Megaworld Corporation (MEG) | 34% |
| 18 | Manila Electric Company (MER) | 21% |
| 19 | Metro Pacific Investments Corp (MPI) | 42% |
| 20 | Petron Corporation (PCOR) | 24% |
| 21 | Puregold Price Club, Inc. (PGOLD) | 33% |
| 22 | Robinsons Land Corporation (RLC) | 39% |
| 23 | Robinsons Retail Holdings, Inc. (RRHI) | 38% |
| 24 | Semirara Mining and Power Corporation (SCC) | 26% |
| 25 | Security Bank Corporation (SECB) | 59% |
| 26 | SM Investments Corporation (SM) | 44% |
| 27 | San Miguel Corporation (SMC) | 15% |
| 28 | SM Prime Holdings, Inc. (SMPH) | 31% |
| 29 | PLDT, Inc. (TEL) | 50% |
| 30 | Universal Robina Corporation (URC) | 44% |

4. Gathered data on the top 100 stockholders of each of the 30 PSEi-indexed stocks from the PSE EDGE portal⁷ to get additional information regarding the top stockholders of each company covered in the study.
5. Computed the percentage of the voting shares of controlling stockholders based on the information taken from the annual report and the Top 100 stockholders from PSE EDGE portal.
6. Gathered data regarding the public float of each of the stocks covered in the study from the PSE EDGE portal.
7. Reviewed relevant articles related to corporate governance especially those related to listed Philippine companies.
8. Assessed the adequacy of existing rules and the practices of the 30 PSEi-indexed stocks in protecting the interest of minority stockholders.

5 Findings

The findings of this study are grouped into the following sections: ownership structure, the positions of chairman of the Board and chief executive officer (CEO) being held by different individuals, independent directors and related party transactions.

5.1 Ownership Structure

Table 2 presents information regarding the identified biggest stockholders behind each of the 30 PSEi-indexed stocks and their respective percentage share in the voting stocks of these companies.

⁷ <http://edge.pse.com.ph/>

Table 2. Identified Biggest Stockholders of the PSEi-Indexed Stocks and their Estimated % Share in the Voting Stocks (Both Common Stocks and Preferred Stocks)

| | Company | Biggest Stockholders | Estimated % Share in the Voting Stocks of Biggest Stockholders as of Dec. 31, 2017 ⁸ |
|----|--|--|---|
| 1 | Ayala Corporation (AC) | MERMAC, Inc. | 56.00% |
| 2 | Aboitiz Equity Ventures (AEV) | Aboitiz & Co., Inc. and related parties | 56.10% |
| 3 | Alliance Global, Inc. (AGI) | The Andresons Group, Inc. And related parties | 55.29% |
| 4 | Ayala Land Inc. (ALI) | Ayala Corporation | 68.56% |
| 5 | Aboitiz Power Corporation (AP) | Aboitiz Equity Ventures, Inc. (AEV) | 76.88% |
| 6 | BDO Unibank, Inc. (BDO) | SM Investments Corp (SM) and related parties | 54.52% |
| 7 | Bank of the Philippine Islands (BPI) | Ayala Corporation and related parties | 50.60% |
| 8 | DMCI Holdings, Inc. (DMC) | Dacon Corporation and related parties | 69.44% |
| 9 | First Gen Corporation (FGEN) | First Philippine Holdings Corporation (FPH) | 66.76% |
| 10 | Globe Telecom, Inc. (GLO) | Ayala Corporation (AC) and related parties | 68.51% |
| 11 | GT Capital Holdings | Grand Titan Capital Holdings, Inc. and related parties | 75.83% |
| 12 | International Container Terminal Services, Inc. (ICTS) | Razon Group and related parties | 61.29% |
| 13 | Jollibee Foods Corporation (JFC) | Hyper Dynamic Corporation and the related Tan Caktiong companies | 54.86% |
| 14 | JG Summit Holdings, Inc. (JGS) | Gokongwei Cos. And related parties | 57.93% |
| 15 | LT Group, Inc. (LTG) | Tangent Holdings Corp. | 74.39% |
| 16 | Metropolitan Bank and Trust Company (MBT) | GT Capital Holdings, Inc. and related parties | 42.94% |
| 17 | Megaworld Corporation (MEG) | Alliance Global Group, Inc. and related parties | 67.36% |
| 18 | Manila Electric Company (MER) | Beacon Electric Asset Holdings, Inc. and MPI | 45.46% |
| 19 | Metro Pacific Investments Corp (MPI) | Metro Pacific Holdings, Inc. (MPHI) | 55.00% |
| 20 | Petron Corporation (PCOR) | SMC Group | 76.06% |
| 21 | Puregold Price Club, Inc. (PGOLD) | Cosco Capital, Inc. and related parties | 67.00% |
| 22 | Robinsons Land Corporation (RLC) | JGS and related parties | 61.50% |
| 23 | Robinsons Retail Holdings, Inc. (RRHI) | JE Holdings, Inc. and other Gokongwei parties | 65.00% |
| 24 | Semirara Mining and Power Corporation (SCC) | DMCI and related parties | 69.09% |
| 25 | Security Bank Corporation (SECB) | Frederick and Daniel Dy | 32.87% |
| 26 | SM Investments Corporation (SM) | Sy and affiliated companies and family members | 55.70% |
| 27 | San Miguel Corporation (SMC) | Top Frontier Investment Holdings, Inc. and Privado Holdings, Corp. | 81.49% |
| 28 | SM Prime Holdings, Inc. (SMPH) | Directors, officers and Sy affiliated companies | 68.42% |
| 29 | PLDT, Inc. (TEL) | First Pacific Group and BTF Holdings, Inc. | 56.07% |
| 30 | Universal Robina Corporation (URC) | JG Summit Holdings, Inc. | 55.13% |

⁸ The biggest stockholders were identified from the Top 100 stockholders submitted by each company to PSE and disclosed at PSE.EDGE. To compute the estimated % share in the voting stocks, the sum of the common stocks and the voting preferred stocks identified by the controlling stockholders were divided by the sum of the total common stocks and voting preferred stocks of each company covered in the study.

Table 3 shows the nine (9) PSEi-indexed stocks which have voting preferred stocks.

Table 3. List of PSEi-Indexed Stocks with Voting Preferred Stocks

| | |
|---|--|
| 1 | Ayala Corporation (AC) |
| 2 | Ayala Land Inc. (ALI) |
| 3 | Globe Telecom, Inc. (GLO) |
| 4 | GT Capital Holdings |
| 5 | International Container Terminal Services, Inc. (ICTS) |
| 6 | Megaworld Corporation (MEG) |
| 7 | Metro Pacific Investments Corp (MPI) |
| 8 | Security Bank Corporation (SECB) |
| 9 | PLDT, Inc. (TEL) |

In general, these voting preferred stocks are not listed and are issued to and held by related parties. Of the nine voting preferred stocks, only Globe preferred shares are listed which probably have not even traded since their listing as shown in PSE website where the issue date and last date traded are the same, June 29, 2001. There are 158,515,021 shares. Of this amount, 158,515,016 are held by Asiacom Philippines, Inc., a company which is 60% owned by Ayala Corporation and 40% owned by Singapore Telecom International.

In the case of PLDT, the 150 million voting preferred shares were subscribed by BTF Holdings, Inc. (BTFHI), a wholly-owned company of the Board of Trustees for the account of the Beneficial Trust Fund or PLDT Trust Funds, which was created pursuant to PLDT's Benefit Plan. The total subscription price was at par value of PHP1.00 per share or a total of PHP 150 million and the shares account for almost 41% of the total voting stocks of PLDT. The issuance of these voting preferred stocks was PLDT's response to address the foreign ownership issue which was raised against the company in 2011. The Philippine Constitution requires maximum 40% ownership of a telecom company by foreign investors.

These voting preferred stocks which account for 16% to 57% of the voting stocks of the nine listed companies were issued at prices much lower than the common stocks. For example, the voting preferred stocks of Globe Telecom which represent more than 54% of the company's voting stocks were issued for a total consideration of about PHP800 million. If the same controlling interest were to be paid for the common stocks of Globe Telecom, more than PHP88 billion would have been paid by an investor given its closing price of PHP556 on June 29, 2001, the date these voting preferred stocks were issued.

In the case of PLDT, the voting preferred stocks account for almost 41% of the total voting stocks. If the same voting percentage were to be acquired by an investor on the company's common stocks on March 22, 2012, the date these voting preferred stocks were issued, an investor would have paid PHP390 billion based on PLDT's closing price of PHP2,600 per share on that date.

Table 4 presents a summary of the amount invested by the voting preferred stockholders and their percentage share in the total voting stocks of each of the nine (9) listed companies.

Table 4. List of PSEi-Indexed Stocks with Voting Preferred Stocks

| | Company | % of Voting P/S to Total Voting Stocks (As of Dec. 31, 2017)⁹ | Cost to P/S Stockholders (in PHP, Except for ICTS) |
|---|--|---|---|
| 1 | Ayala Corporation (AC) | 24.35% | 200,000,000 |
| 2 | Ayala Land Inc. (ALI) | 47.02% | 1,306,649,000 |
| 3 | Globe Telecom, Inc. (GLO) | 54.39% | 792,575,105 |
| 4 | GT Capital Holdings | 47.51% | 17,430,000 |
| 5 | International Container Terminal Services, Inc. (ICTS) | 25.57% | US\$140,000 |
| 6 | Megaworld Corporation (MEG) | 15.69% | 60,000,000 |
| 7 | Metro Pacific Investments Corp (MPI) | 22.46% | 91,281,053 |
| 8 | Security Bank Corporation (SECB) | 57.03% | 100,000,000 |
| 9 | PLDT, Inc. (TEL) | 40.98% | 150,000,000 |

Except for Ayala Corporation, Ayala Land, Inc. and GT Capital Holdings, the pre-emptive right of the common stockholders was waived for the offering of these voting preferred stocks.¹⁰

5.2 Decisions Which Require At Least 2/3 Votes from the Stockholders

There are certain corporate decisions that need super majority vote of the stockholders to be carried out. Super majority vote means at least 2/3 of the voting stocks. If the controlling stockholders do not have at least 2/3 of the voting stocks, then, there may be some decisions they want to undertake, such as an acquisition of another company, which can be blocked by the minority stockholders if the latter do not approve of such plan.

Based on the Revised Corporation Code of the Philippines, the following are examples of decisions that need super majority vote:

Section 15. Amendment of Articles of Incorporation.

Section 27. Removal of directors.

Section 36. Extension or shortening of corporate term.

Section 37. Increase or decrease in capital stock

Section 38. Denial of pre-emptive right (which will be discussed in detail later on)

Section 39. Sale or other disposition of assets.

Section 41. Investment of corporate funds in another corporation or business or for any other purpose.

Section 47. Amendments to by-laws.

Section 76. Merger and consolidation

The minimum float requirement for companies planning to have initial public offerings has been increased to 20% from 10%. However, the existing listed companies which are not covered by the new requirement can keep their minimum public float of 10%. These minimum float requirements, even the 20%, are way below the 33 and 1/3% minority vote required by the Corporation Code to block certain decisions of the majority stockholders.

Based on the non-float shares¹¹ computed from the information provided in Table 1, the controlling stockholders of 18 of the 30 PSE-indexed companies do not have supermajority vote.

⁹ This is computed by dividing the number of voting preferred stocks by the sum of common stocks and voting preferred stocks. Each voting preferred stock has one vote which is equivalent to the voting right of a common stock.

¹⁰ This conclusion was based on the examination of the notes to financial statements on equity of the nine companies covered in this study.

¹¹ Nonfloat shares = 100% - Public Float %

Table 2 shows that the identified biggest stockholders of 13 of the 30 PSE-indexed stocks have supermajority vote. Two of these 13 companies (ALI and GTCAP) managed to have supermajority vote through their voting preferred stocks. Ayala Land, Inc. (ALI) has a public float of 52% on common stocks but controlling stockholders have 68.56% of the total voting stocks. GT Capital Holdings (GTCAP) has 44% public float on common stocks but its controlling stockholders have 75.83% of the total voting stocks (see Tables 1 and 2).

5.3 Positions of Chairman and CEO Being Held by Separate Individuals

Recommendation 5.4 of the Code of Corporate Governance for Publicly-Listed Companies suggests that the positions of chairman of the board and chief executive officer (CEO) be held by separate individuals. Table 5 presents a summary of whether these positions are held by separate individuals in the companies covered in this study.

Table 5. Summary of Chairman and CEO/President Being Assigned to Different Individuals As of December 31, 2017

| | Company | Separate Chairman and President/CEO ¹² |
|----|--|---|
| 1 | Ayala Corporation (AC) | X |
| 2 | Aboitiz Equity Ventures (AEV) | ✓ |
| 3 | Alliance Global, Inc. (AGI) | ✓ |
| 4 | Ayala Land Inc. (ALI) | ✓ |
| 5 | Aboitiz Power Corporation (AP) | ✓ |
| 6 | BDO Unibank, Inc. (BDO) | ✓ |
| 7 | Bank of the Philippine Islands (BPI) | ✓ |
| 8 | DMCI Holdings, Inc. (DMC) | X |
| 9 | First Gen Corporation (FGEN) | X |
| 10 | Globe Telecom, Inc. (GLO) | ✓ |
| 11 | GT Capital Holdings | ✓ |
| 12 | International Container Terminal Services, Inc. (ICTS) | X |
| 13 | Jollibee Foods Corporation (JFC) | ✓ |
| 14 | JG Summit Holdings, Inc. (JGS) | X |
| 15 | LT Group, Inc. (LTG) | X |
| 16 | Metropolitan Bank and Trust Company (MBT) | ✓ |
| 17 | Megaworld Corporation (MEG) | ✓ |
| 18 | Manila Electric Company (MER) | ✓ |
| 19 | Metro Pacific Investments Corp (MPI) | ✓ |
| 20 | Petron Corporation (PCOR) | ✓ |
| 21 | Puregold Price Club, Inc. (PGOLD) | ✓ |
| 22 | Robinsons Land Corporation (RLC) | ✓ |
| 23 | Robinsons Retail Holdings, Inc. (RRHI) | X |
| 24 | Semirara Mining and Power Corporation (SCC) | X |
| 25 | Security Bank Corporation (SECB) | ✓ |
| 26 | SM Investments Corporation (SM) | ✓ |
| 27 | San Miguel Corporation (SMC) | X |
| 28 | SM Prime Holdings, Inc. (SMPH) | ✓ |
| 29 | PLDT, Inc. (TEL) | X |
| 30 | Universal Robina Corporation (URC) | ✓ |

¹² X means the positions of the Chairman of the Board of Directors and CEO or its equivalent are held by the same person.

Ten (10) of the companies in this study have the positions of the chairman of the board of directors and CEO being assigned to the same individual. But even the companies where both positions were assigned to different individuals, the persons assigned to the positions come mostly from the same group of controlling stockholders, or members of the family controlling the company.

Twenty one (21) or 70% of the PSE-indexed companies covered in this study were identified to have controlling stockholders or members of their families occupying top executive positions in the companies they control (see Table 6).

Table 6. List of Companies Where Controlling Stockholders or Members of their Families Occupy Top Executive Positions (As of December 31, 2017)

| | Company | Controlling Stockholders or Family Members Occupying Top Executive Positions | Position/s |
|----|--|---|--------------------------|
| 1 | Ayala Corporation (AC) | Jaime Augusto Zobel de Ayala Fernando Zobel de Ayala | CEO President and COO |
| 2 | Aboitiz Equity Ventures (AEV) | Erramon Aboitiz | President and CEO |
| 3 | Alliance Global, Inc. (AGI) | Kevin Andrew Tan | Executive Director |
| 4 | Aboitiz Power Corporation (AP) | Antonio R. Moraza | President and COO |
| 5 | DMCI Holdings, Inc. (DMC) | Isidro A. Consunji | CEO and President |
| 6 | First Gen Corporation (FGEN) | Federico R. Lopez | CEO |
| 7 | GT Capital Holdings | Anjanette Ty Dy-Buncio | Treasurer |
| 8 | International Container Terminal Services, Inc. (ICTS) | Enrique K. Razon, Jr. | President |
| 9 | Jollibee Foods Corporation (JFC) | Ernesto Tanmantiong | CEO and President |
| 10 | JG Summit Holdings, Inc. (JGS) | James Go Lance Y. Gokongwei | President COO |
| 11 | LT Group, Inc. (LTG) | Lucio C. Tan Michael G. Tan | CEO President |
| 12 | Megaworld Corporation (MEG) | Andrew L. Tan | President |
| 13 | Petron Corporation (PCOR) | Ramon S. Ang | President |
| 14 | PLDT, Inc. (TEL) | Manuel V. Pangilinan | CEO and President |
| 15 | Robinsons Land Corporation (RLC) | Lance Y. Gokongwei | CEO |
| 16 | Robinsons Retail Holdings, Inc. (RRHI) | Lance Y. Gokongwei Robina Gokongwei-Pe | CEO President |
| 17 | Semirara Mining and Power Corporation (SCC) | Isidro A. Consunji Victor A. Consunji | CEO President |
| 18 | Security Bank Corporation (SECB) | Anastacia Y. Dy | Executive Director |
| 19 | SM Investments Corporation (SM) | Harley T. Sy | Executive Director |
| 20 | San Miguel Corporation (SMC) | Ramon S. Ang | President and COO |
| 21 | Universal Robina Corporation (URC) | Lance Y. Gokongwei | CEO and President |

In the case of PLDT, Manuel V. Pangilinan is not a member of the Salim family which controls First Pacific Company Limited, the biggest common stockholder of PLDT. However, he represents BTF Holdings, Inc. which owns all the voting preferred stocks issued by PLDT. These voting preferred stocks account for about 41% of all the voting stocks.

5.4 Independent Directors¹³

Recommendation 1.2 of the Code of Corporate Governance for Publicly Listed Companies suggests that the board be composed of a majority of competent and qualified non-executive directors (NEDs) to provide better management decisions and check and balance (see Appendix A for the attributes of an independent director). A good combination of NEDs which should include independent directors prevents a director or a small group of directors from dominating the decision-making process.

Table 7 provides a summary of the number of independent directors of the 30 companies covered in this study.

Table 7. Number and Percentage of Independent Directors to Total Directors (As of December 31, 2017)

| | Company | No. of Directors | No. of Independent Directors | % of Independent Directors to Total Directors |
|----|--|------------------|------------------------------|---|
| 1 | Ayala Corporation (AC) | 7 | 2 | 28.57% |
| 2 | Aboitiz Equity Ventures (AEV) | 9 | 3 | 33.33% |
| 3 | Alliance Global, Inc. (AGI) | 7 | 2 | 28.57% |
| 4 | Ayala Land Inc. (ALI) | 9 | 3 | 33.33% |
| 5 | Aboitiz Power Corporation (AP) | 9 | 3 | 33.33% |
| 6 | BDO Unibank, Inc. (BDO) | 14 | 5 | 35.71% |
| 7 | Bank of the Philippine Islands (BPI) | 15 | 6 | 40.00% |
| 8 | DMCI Holdings, Inc. (DMC) | 9 | 2 | 22.22% |
| 9 | First Gen Corporation (FGEN) | 9 | 3 | 33.33% |
| 10 | Globe Telecom, Inc. (GLO) | 11 | 3 | 27.27% |
| 11 | GT Capital Holdings | 13 | 3 | 23.08% |
| 12 | International Container Terminal Services, Inc. (ICTS) | 7 | 2 | 28.57% |
| 13 | Jollibee Foods Corporation (JFC) | 9 | 2 | 22.22% |
| 14 | JG Summit Holdings, Inc. (JGS) | 11 | 3 | 27.27% |
| 15 | LT Group, Inc. (LTG) | 13 | 4 | 30.77% |
| 16 | Metropolitan Bank and Trust Company (MBT) | 13 | 6 | 46.15% |
| 17 | Megaworld Corporation (MEG) | 7 | 3 | 42.86% |
| 18 | Manila Electric Company (MER) | 11 | 2 | 18.18% |
| 19 | Metro Pacific Investments Corp (MPI) | 14 | 3 | 21.43% |
| 20 | Petron Corporation (PCOR) | 15 | 3 | 20.00% |
| 21 | Puregold Price Club, Inc. (PGOLD) | 12 | 3 | 25.00% |
| 22 | Robinsons Land Corporation (RLC) | 11 | 4 | 36.36% |
| 23 | Robinsons Retail Holdings, Inc. (RRHI) | 9 | 2 | 22.22% |
| 24 | Semirara Mining and Power Corporation (SCC) | 11 | 2 | 18.18% |
| 25 | Security Bank Corporation (SECB) | 15 | 6 | 40.00% |
| 26 | SM Investments Corporation (SM) | 9 | 2 | 22.22% |
| 27 | San Miguel Corporation (SMC) | 15 | 3 | 20.00% |
| 28 | SM Prime Holdings, Inc. (SMPH) | 9 | 3 | 33.33% |
| 29 | PLDT, Inc. (TEL) | 13 | 3 | 23.08% |
| 30 | Universal Robina Corporation (URC) | 9 | 2 | 22.22% |

¹³ The Code of Corporate Governance for Publicly Listed Companies defines independent director as a person who is independent of management and the controlling shareholder, and is free from any business or other relationship which could, or could reasonably be perceived to, materially interfere with his exercise of independent judgment in carrying out his responsibilities as a director.

As shown in Table 7, all companies satisfied the previous requirement of having at least two independent directors in the Board. However, Recommendation 5.1 of the 2016 Revised Code of Corporate Governance for Publicly Listed Companies increased the minimum number to three, or a number as to constitute at least one-third of the members of the Board, whichever is higher.

While all the companies in this study discussed the procedures they adopted in nominating directors, including independent directors, the general practice is that the controlling stockholders significantly influence the nomination. Having majority of the voting shares allow them to nominate more. The power to nominate a director and have the nominee elected in the board is based on the number of voting shares a stockholder has.

Since the controlling stockholders are also actively involved in management, they can approach possible nominees to become independent directors.

Non-executive directors, including the independent directors, get some remuneration for attending board meetings. Given the way independent directors are nominated and the benefits they get from being directors, one will begin to wonder how independent these independent directors are. There can be moral hazard issues in this situation.

5.5 Related Party Transactions

The following paragraphs are taken from Recommendation 2.7 of the Code of Corporate Governance for Publicly-Listed Companies.

“The Board should have the overall responsibility in ensuring that there is a group-wide policy and system governing related party transactions (RPTs) and other unusual or infrequently occurring transactions, particularly those which pass certain thresholds of materiality. The policy should include the appropriate review and approval of material or significant RPTs, which guarantee fairness and transparency of the transactions. The policy should encompass all entities within the group, taking into account their size, structure, risk profile and complexity of operations.”

“Ensuring the integrity of related party transactions is an important fiduciary duty of the director. It is the Board’s role to initiate policies and measures geared towards prevention of abuse and promotion of transparency, and in compliance with applicable laws and regulations to protect the interest of all shareholders. One such measure is the required ratification by shareholders of material or significant RPTs approved by the Board, in accordance with existing laws. Other measures include ensuring that transactions occur at market prices, at arm’s-length basis and under conditions that protect the rights of all shareholders.”

For this section, private placements offered at a discount, issuance of voting preferred stocks to related companies, transfer of assets to related parties, and tender offers are cited as examples where the interest of minority stockholders was violated.

Cayanan (2017) concluded that on the average, minority stockholders suffered losses from private placements issued by listed Philippine companies. Based on 17 samples, the average discount of the private placement offer price was 5.34% when compared to the closing price a day prior to the announcement. If the effects of the four companies offered at a premium were to be taken out, the average discount would increase to 10.72%. Table 8 shows an excerpt of the study showing examples of private placements conducted by PSEi-indexed stocks offered at a discount.

Table 8. Examples of Private Placements Offered by PSEi-Indexed Stocks at a Discount

| | Private Placement (PP) Announcement Date | PP Offer Price | Stock Price a Day Prior to Announcement | PP Discount |
|-----------------------------|---|-----------------------|--|--------------------|
| Ayala Corporation | November 20, 2014 | 660 | 717 | -7.95% |
| Ayala Land, Inc. | January 12, 2015 | 33 | 35 | -5.71% |
| First Gen | January 21, 2015 | 25.25 | 26 | -2.88% |
| GT Capital | February 3, 2015 | 1,130.00 | 1,180.00 | -4.24% |
| JG Summit Holdings, Inc. -1 | January 21, 2015 | 61 | 70.05 | -12.92% |
| JG Summit Holdings, Inc. -2 | February 2, 2012 | 25 | 28.35 | -11.82% |

| | Private Placement (PP) Announcement Date | PP Offer Price | Stock Price a Day Prior to Announcement | PP Discount |
|------------------------|--|-------------------|--|----------------|
| Metro Pacific - 1 | February 10, 2015 | 4.9 | 5.24 | -6.49% |
| Metro Pacific -2 | January 23, 2013 | 4.6 | 4.91 | -6.31% |
| Metro Pacific -3 | July 9, 2011 | 3.6 | 3.79 | -5.01% |
| Petron Corp. | March 28, 2014 | 11.5 | 13.4 | -14.18% |
| SM Investments Corp. | August 2, 2013 | 900 | 961.5 | -6.40% |
| Universal Robina Corp. | October 4, 2013 | 115 | 116 | -0.86% |

The four companies which offered their private placement offer prices at a premium were Megaworld Corporation (9.11% premium), Global Estate Resorts Inc. (18.32% premium), RCBC Bank (19.40% premium) and Universal Robina Corporation (1.64% premium) for its 2012 private placement.

Private placements are allowed under Section 38 of the Revised Corporation Code of the Philippines, stated as follows:

*Section 38. Power to deny pre-emptive right. All stockholders of a stock corporation shall enjoy pre-emptive right to subscribe to all issues or disposition of shares of any class, in proportion to their respective shareholdings, **unless such right is denied** by the articles of incorporation or an amendment thereto: Provided, that such pre-emptive right shall not extend to shares to be issued in compliance with laws requiring stock offerings or minimum stock ownership by the public; or to shares to be issued in good faith with the approval of the stockholders representing **two-thirds (2/3)** of the outstanding capital stock, in exchange for property needed for corporate purposes or in payment of a previously contracted debt.*

Offering new shares through private placements at a discount dilutes the interest of minority stockholders. But while these private placements are oftentimes dilutive, offering preferred stocks with voting rights at very low prices relative to the common stocks' prices is even more dilutive. Non-listing of these voting preferred stocks further aggravates the situation because minority stockholders are not even given the opportunity to participate in these offers (see Table 4).

Tender offers and voluntary delisting can also be disadvantageous to minority stockholders. Liberty Telecoms, a subsidiary of San Miguel Corporation (SMC), conducted a tender offer in 2016 amidst complaints from some minority stockholders. The offer price of PHP2.20 was considered low by minority stockholders considering Liberty Telecom's valuable telco frequencies including those in the 700 Megahertz band (Camus, October 2016). A security firm valued Liberty stock at PHP5.00 per share with its frequencies (Camus, September 2016).

Liberty's telecom frequencies were transferred through its subsidiary, Tori Spectrum Telecom, Inc., to Vega's Bell Telecommunications, Inc., an affiliated company, in March 2015. The transaction was disclosed in 2016 when the company applied for tender offer. SEC fined the company PHP346,000 for violating disclosure requirements (Camus, 2016).

Vega Telecom of SMC was sold to Globe Telecom and PLDT for PHP70 billion in March 2017. The main subject of the valuation was the telecom frequency.

6 Conclusion

The findings of this study show that the welfare of the minority stockholders is anchored on the management prudence of controlling stockholders. Widespread ownership base of listed companies which may be true for some developed economies is not evident among listed Philippine companies. This situation creates agency problems between the controlling and minority stockholders.

The presence of majority stockholders who are actively involved in management is consistent with the findings of Claessens et al. (2000). Their study which included several companies from East Asian countries, showed that the separation of management from ownership control was rare. The

management of 60% of the firms that were not widely held was related to the family of the controlling stockholder.¹⁴

The rules on corporate governance and the implementation of such rules have to be strengthened. While SEC decided to increase the minimum requirement of public float to 20% for new initial public offerings (IPOs), this requirement is still very low, considering that this percentage is way below the blocking minority prescribed in the Corporation Code of the Philippines which is 33 and one-third percent. For those which are already listed, the minimum float remains at 10%. There are certain decisions such as the acquisition and sale of another company which require a super majority vote. This probably explains why most controlling stockholders prefer to have voting shares considerably higher than 50%.

The minimum float requirement of 10% for already listed companies and 20% for new IPOs is significantly weakened if SEC does not monitor the issuance of voting preferred stocks. Allowing the issuance of these unlisted voting preferred stocks which are dilutive to minority stockholders is a lapse in regulation. This situation can potentially aggravate the agency problems between the controlling and minority stockholders.

To address this issue, SEC and PSE should increase the minimum public float to at least 33 and one-third percent, and should cover all voting shares. This suggests that the companies which have issued voting preferred stocks must be required to list them.

While the Corporation Code of the Philippines allows private placements, shouldn't the regulators require that these private placements be offered at a premium? If this cannot be done, shouldn't the listed companies be required to offer the new shares through a stock rights offering where all stockholders will be given equal opportunity to subscribe? This process definitely takes more time but this is a small price to pay for having a better access to capital markets.

The presence and nomination of independent directors is another concern. How independent are these independent directors? If they are nominated by the controlling stockholders and receive benefits in the process, can they really be independent? This is an area of corporate governance that is difficult to assess. However, if the votes of each member of the Board will be required by SEC and PSE to be disclosed, especially on issues that affect the welfare of minority stockholders such as private placements, tender offers or material related party transactions, then, maybe, they will think twice before they vote.

The move to increase the number of independent directors in the Board is a positive development. But this will be more meaningful if the choice of independent directors will come from the minority stockholders, and not from the majority stockholders. SEC and PSE should come up with guidelines towards this direction.

There are other issues adversely affecting minority stockholders such as forced delisting of companies or prolonged suspension of companies from trading, which were not discussed in this paper. While the controlling stockholders and managers of these companies deserve to be penalized for non-compliance, mostly related to reportorial requirements, the minority stockholders suffer more for decisions beyond their control. These cases and the issues presented in this paper are reflections of a corporate governance system that is far from ideal. This situation may partly explain why the Philippine stock market which was established in 1927 and one of the oldest exchanges in Asia, remains one of the smallest.

¹⁴ There were 2,980 corporations included in the study coming from nine East Asian countries, namely, Hong Kong, Indonesia, Japan, Korea, Malaysia, Philippines, Singapore, Taiwan and Thailand.

References

- Ayala Corporation (2017). *Annual Report*.
- Aboitiz Equity Ventures (2017). *Annual Report*.
- Aboitiz Power Corporation (2017). *Annual Report*.
- Alliance Global, Inc. (2017). *Annual Report*.
- Ayala Land, Inc. (2017). *Annual Report*.
- Batas Pambansa Bilang 68. Corporation Code of the Philippines.
- Bhagat, S. & Black, B. (2002). The non-correlation between board independence and long-term firm performance. *Journal of Corporation Law*, 27, 231-274.
- BDO Unibank, Inc. (2017). *Annual Report*.
- Bank of the Philippine Islands (2017). *Annual Report*.
- Camus, M.R. (2016, October 22). Corporate watchdog slaps fine on liberty telecoms for non-disclosure. *Philippine Daily Inquirer*, Retrieved from <https://business.inquirer.net/217149/corporate-watchdog-slaps-fine-on-liberty-telecoms-for-non-disclosure>
- Camus, M.R. (2016, September 14). SMC explains Liberty Telecom move. *Philippine Daily Inquirer*, Retrieved from <https://business.inquirer.net/214860/smc-explains-liberty-telecom-move>
- Cayanan, A. (2017). Private placements and the minority interests: The Philippine case. *Philippine Management Review*, 24, 49-62.
- Cayanan, A. (2018). *Corporate Governance Issues in Listed Philippine Companies* [PowerPoint presentation]. Retrieved from http://www.bsp.gov.ph/events/pcls/downloads/2018/BSP_5b_cayanan_presentation.pdf
- Claessens, S., Djankov, S., Fan, J. & Lang, L. (1999). *Expropriation of Minority Shareholders: Evidence from East Asia*. (Policy Research Paper 2088). World Bank, Washington DC. Retrieved from <http://documents.worldbank.org/curated/en/283121468771272365/pdf/multi-page.pdf>
- Claessens, S., Djankov, S. & Lang, L. (2000). The separation of ownership and control in East Asian corporations. *Journal of Financial Economics*, 58(1-2), 81-112.
- DMCI Holdings, Inc. (2017). *Annual Report*.
- Desender, K. (2009). *The relationship between the ownership structure and the role of the board*. (Working Paper). Retrieved from http://www.business.illinois.edu/Working_Papers/papers/09-0105.pdf
- Echanis, E. (2006). Philippine corporate governance: issues and reforms. *Philippine Management Review*, 13, 21-41.
- Fernández-Rodríguez, E. Gómez-Ansón & Cuervo-García (2004). The stock market reaction to the introduction of best practices codes by Spanish firms. *Corporate Governance: An International Review*, 12(1), 29-45.
- First Gen Corporation (2017). *Annual Report*.
- Globe Telecom, Inc. (2017). *Annual Report*.
- Gourevitch, P. (2003). The politics of corporate governance regulation. *Yale Law Journal*, 112, 1829-1880.
- GT Capital Holdings (2017). *Annual Report*.
- International Container Terminal Services, Inc. (2017). *Annual Report*.
- Jensen, M. (1993). The modern industrial revolution, exit, and the failure of internal control systems. *The Journal of Finance*, 48(3), 831-880.
- Jollibee Foods Corporation (2017). *Annual Report*.
- JG Summit Holdings, Inc. (2017). *Annual Report*.
- Johnson, S., Boone, P., Breach, A. & Friedman, E. (2000). Corporate governance in the Asian financial crisis. *Journal of Financial Economics*, 58(1-2), 141-186.
- Kaplan, S. (1994). Top executive rewards and firm performance: A comparison of Japan and the United States. *Journal of Political Economy*, 102, 510-546.
- La Porta, R., Lopez-de-Silanes, F. & Shleifer, A. (1999). Corporate ownership around the world. *The Journal of Finance*, 54(2), 471-517.
- La Porta, R., Lopez-de-Silanes, F., Shleifer, A. & Vishny, R. (2000). Investor protection and corporate governance. *Journal of Financial Economic*, 58(1-2), 3-27.
- LT Group, Inc. (2017). *Annual Report*.

- Metropolitan Bank and Trust Company (2017). *Annual Report*.
- Megaworld Corporation (2017). *Annual Report*.
- Manila Electric company (2017). *Annual Report*.
- Metro Pacific Investments, Corp. (2017). *Annual Report*.
- Noll, R. (1989). Economic perspectives on the politics of regulation. *Handbook of Industrial Revolution*, 2, 1253-1287. Retrieved from <https://www.sciencedirect.com/science/article/pii/S1573448X89020108>
- Petron Corporation (2017). *Annual Report*.
- Pritchard, A. (2009). Monitoring of corporate groups by independent directors. *Journal of Korean Law*, 9, 1-25.
- Puregold Price Club, Inc. (2017). *Annual Report*.
- Republic Act No. 11232. An Act Providing for the Revised Corporation Code of the Philippines.
- Robinsons Land Corporation (2017). *Annual Report*.
- Robinsons Retail Holdings, Inc. (2017). *Annual Report*.
- Roe, M. (2019). Corporate Law's Limits. [online] Dash.harvard.edu. Retrieved from <https://dash.harvard.edu/handle/1/12206465>
- SEC Memorandum Circular No. 19, Series of 2016. Code of corporate governance for publicly-listed companies. Retrieved from http://www.sec.gov.ph/wp-content/uploads/2016/12/2016_memo_circular_no.19.pdf
- Semirara Mining and Power Corporation (2017). *Annual Report*.
- Security Bank Corporation (2017). *Annual Report*.
- Shleifer, A. & Vishny, R. (1997). A survey of corporate governance. *The Journal of Finance*, 52(2), 737-783.
- SM Investments Corporation (2017). *Annual Report*.
- San Miguel Corporation (2017). *Annual Report*.
- SM Prime Holdings, Inc. (2017). *Annual Report*.
- PLDT, Inc. (2017). *Annual Report*.
- Universal Robina Corporation (2017). *Annual Report*.
- Walsh, J. & Seward, J. (1990). On the efficiency of internal and external corporate control mechanism. *Academy of Management Review*, 15(3), 421-458.

Appendix A

Attributes of an Independent Director (Recommendation 5.2 of the Code of Corporate Governance for Publicly Listed Companies)

An Independent Director refers to a person who, ideally:

- a. Is not, or has not been a senior officer or employee of the covered company unless there has been a change in the controlling ownership of the company;
- b. Is not, and has not been in the three years immediately preceding the election, a director of the covered company; a director, officer, employee of the covered company's subsidiaries, associates, affiliates or related companies; or a director, officer, employee of the covered company's substantial shareholders and its related companies;
- c. Has not been appointed in the covered company, its subsidiaries, associates, affiliates or related companies as Chairman "Emeritus," "Ex-Officio" Directors/Officers or Members of any Advisory Board, or otherwise appointed in a capacity to assist the Board in the performance of its duties and responsibilities within three years immediately preceding his election;
- d. Is not an owner of more than two percent (2%) of the outstanding shares of the covered company, its subsidiaries, associates, affiliates or related companies;
- e. Is not a relative of a director, officer, or substantial shareholder of the covered company or any of its related companies or of any of its substantial shareholders. For this purpose, relatives include spouse, parent, child, brother, sister and the spouse of such child, brother or sister;
- f. Is not acting as a nominee or representative of any director of the covered company or any of its related companies;
- g. Is not a securities broker-dealer of listed companies and registered issuers of securities. "Securities broker-dealer" refers to any person holding any office of trust and responsibility in a broker-dealer firm, which includes, among others, a director, officer, principal stockholder, nominee of the firm to the Exchange, an associated person or salesman, and an authorized clerk of the broker or dealer;
- h. Is not retained, either in his personal capacity or through a firm, as a professional adviser, auditor, consultant, agent or counsel of the covered company, any of its related companies or substantial shareholder, or is otherwise independent of Management and free from any business or other relationship within the three years immediately preceding the date of his election;
- i. Does not engage or has not engaged, whether by himself or with other persons or through a firm of which he is a partner, director or substantial shareholder, in any transaction with the covered company or any of its related companies or substantial shareholders, other than such transactions that are conducted at arm's length and could not materially interfere with or influence the exercise of his independent judgment;
- j. Is not affiliated with any non-profit organization that receives significant funding from the covered company or any of its related companies or substantial shareholders; and
- k. Is not employed as an executive officer of another company where any of the covered company's executives serve as directors.