

SIXTEENTH CONGRESS OF THE REPUBLIC)
OF THE PHILIPPINES)
First Regular Session)



'14 MAR 11 P5 01

SENATE
S.B. NO. 2175

RECEIVED BY: *ji*

Introduced by Senator Maria Lourdes Nancy S. Binay

AN ACT CLARIFYING THE REQUIREMENTS FOR ENGAGING IN ACTIVITIES COVERED BY THE SECONDARY PURPOSE CLAUSE OF CORPORATIONS, AMENDING BATAS PAMBANSA BLG. 68 OTHERWISE KNOWN AS THE CORPORATION CODE OF THE PHILIPPINES

EXPLANATORY NOTE

Pursuant to the Corporation Code of the Philippines or Batas Pambansa Blg. 68 (the "Corporation Code"), Corporations are allowed to engaged in activities covered by their primary purpose clause/s and secondary purpose clause/s as stated in their Articles of Incorporation.

Despite years of practice under the Corporation Code, there appears to be disagreement as to the requirements for a Corporation to engage in any business and or activity covered by its secondary purpose clause. The reason for this may have to do with the wording of the current Section 42 of the Corporation Code, which appears to be the governing provision insofar as corporate decisions to engage in its secondary purpose clause in concerned. Section 42 provides, to wit:

"Section 42. *Power to invest corporate funds in another corporation or business or for any other purpose.* – Subject to the provisions of this Code, a private corporation may invest its funds in any other corporation or business or for any purpose other than the primary purpose for which it was organized when approved by a majority of the board of directors or trustees and ratified by the stockholders representing at least two-thirds (2/3) of the outstanding capital stock, or by at least two thirds (2/3) of the members in the case of non-stock corporations, at a stockholder's or member's meeting duly called for the purpose. Written notice of the proposed investment and the time and place of the meeting shall be addressed to each stockholder or member at his place of residence as shown on the books of the corporation and deposited to the addressee in the post office with postage prepaid, or served personally: Provided, That any dissenting stockholder shall have appraisal right as provided in this Code: Provided, however, That where the investment by the corporation is reasonably necessary to accomplish its primary purpose as stated in the articles of incorporation, the approval of the stockholders or members shall not be necessary."

The following are key principles that can be implied from the legal text:

1. Subject to the Corporation Code, a private corporation may invest its funds **in another corporation or business** when approved by a majority of the board of directors or trustees and ratified by the stockholders representing at least two-thirds (2/3) of the outstanding capital stock, or by at least two thirds (2/3) of the members in the case of non-stock corporations, at a stockholder's or member's meeting duly called for the purpose. The term "Subject to the Corporation Code" has been interpreted by academics to mean that the investment of funds in another corporation or business should be allowed under the Articles of Incorporation particularly the primary purpose clause of the Corporation. Otherwise, the act of investment may be deemed to be ultra vires under Section 45. (Emphasis supplied.)
2. Subject to the Corporation Code, a private corporation may invest its funds **for any other purpose other than the primary purpose for which it was organized** when approved by a majority of the board of directors or trustees and ratified by the stockholders representing at least two-thirds (2/3) of the outstanding capital stock, or by at least two thirds (2/3) of the members in the case of non-stock corporations, at a stockholder's or member's meeting duly called for the purpose. The term "Subject to the Corporation Code" has been interpreted by academics to refer to the secondary purpose clauses of a Corporation. In other words, if the Corporation has no secondary purpose in its Articles of Incorporation, it cannot invoke this meaning of Section 42. (Emphasis supplied.)

As classified above, Section 42 suffers from the following ambiguities:

First, the provision uses the term "invest" in relation to corporate funds. Black's Law Dictionary (9th Edition, 2009) defines invest to mean "to apply money for profit" or "to make an outlay of money for profit." In other words, the use of corporate funds is used with expectation of profits or returns. As worded, **Section 42 cannot contemplate mere use of funds in pursuit of secondary purposes, where such use is without expectation of profit. It must be noted that Section 42 applies equally to stock and non-stock corporations. In the case of non-stock corporations, corporate funds are used not necessarily for profit.**

Second, Section 42 generally applies to out-of-the-ordinary investments in pursuit of its primary purpose clause. This is the implication of the proviso, which states "That where the investment by the corporation is reasonably necessary to accomplish its primary purpose as stated in the articles of incorporation, the approval of the stockholders or members shall not be necessary." (Emphasis supplied.)

As worded, Section 42 does not provide a rule for all types of engagement of a corporation in activities covered by the secondary purpose clause. Does this mean that for types of activities where there is no expectation of profit, there is no requirement of shareholder or member approval? The provision is silent. This uncertainty gives rise to needless litigations between and among stockholders and stockholders and the corporation.

Section 42 therefore must be clarified. It is suggested that the sound rule should be that Corporations are required to secure prior shareholder or member approval prior to engaging

in activities covered by its secondary purpose clause. The rationale is that corporate funds should be devoted to activities covered by the primary purpose clause, which activities are presumably within the expertise of said Corporation. The reasonable expectation of Shareholders that corporate resources are used for the primary purpose of the Corporation should be protected by law by ensuring that their consent to engage in activities covered by the secondary purpose clause is first secured.

For the above reasons, the passage of this bill is earnestly recommended.


MARIA LOURDES NANCY S. BINAY
Senator

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4 CORPORATION CODE OF THE PHILIPPINES
5
6

7 *Be it enacted by the Senate and House of Representatives of the Philippines in Congress*
8 *assembled:*
9

10 **SECTION 1.** Section 42 of the Corporation Code is hereby amended to read as follows:
11

12 “Section 42. *Power to invest corporate funds in another corporation or business, or [for any*
13 *other purpose.] TO INVEST OR USE OF CORPORATE FUNDS FOR ACTIVITIES*
14 *COVERED BY ITS SECONDARY PURPOSE CLAUSE.* – Subject to the provisions of this
15 Code, a private corporation may, invest its funds in any other corporation or business [or for
16 any purpose other than the primary purpose for which it was organized] AS ALLOWED
17 UNDER ITS PRIMARY PURPOSE CLAUSE; OR INVEST OR USE OF CORPORATE
18 FUNDS FOR ACTIVITIES COVERED BY ITS SECONDARY PURPOSE CLAUSE, when
19 approved by a majority of the board of directors or trustees and ratified by the stockholders
20 representing at least two-thirds (2/3) of the outstanding capital stock, or by at least two thirds
21 (2/3) of the members in the case of non-stock corporations, at a stockholder’s or member’s
22 meeting duly called for the purpose. Written notice of the proposed investment and the time
23 and place of the meeting shall be addressed to each stockholder or member at his place of
24 residence as shown on the books of the corporation and deposited to the addressee in the post
25 office with postage prepaid, or served personally: Provided, That any dissenting stockholder
26 shall have appraisal right as provided in this Code: Provided, however, That where the
27 investment by the corporation is reasonably necessary to accomplish its primary purpose as
28 stated in the articles of incorporation, the approval of the stockholders or members shall not
29 be necessary.
30

31 **SECTION 2.** *Effectivity Clause.* This Act shall take effect fifteen (15) days after its
32 complete publication in at least two (2) newspapers of general circulation.
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34 Approved,