

# BEYOND THE VEIL, INC.: ASSESSING THE VIABILITY OF THE ONE PERSON CORPORATION AS TOOL FOR ESTATE PLANNING \*

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## ABSTRACT

One of the major innovations introduced by the Revised Corporation Code of the Philippines is the One-Person Corporation (OPC) in our jurisdiction. This Note analyzes the viability of the OPC as a potential vehicle for estate planning. The use of corporations as a vehicle to facilitate the intergenerational transfers of wealth is founded on the application of corporation law principles to consolidate wealth for eventual transfer to heirs through the laws of succession. As the first unipersonal corporate form available to private citizens, the use of the OPC as a vehicle for estate planning requires an examination of its applicability for this purpose, as well as the potential challenges such use may face vis-à-vis the existing legal framework of succession. Using official documents of the Philippine legislature, jurisprudence from foreign jurisdiction and other documents, this Note discusses the development of the concept of the unipersonal corporation, its benefits, and potential challenges.

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## INTRODUCTION

### A. One Person Corporation in the Revised Corporation Code

On February 29, 2019, the Revised Corporation Code of the Philippines (“RCC”) was signed into law. This repealed Batas Pambansa Bilang 68 (BP. Blg. 68), commonly known as the Corporation Code of the Philippines, which had been in effect since 1980. The main objectives of the RCC are: (a) improving the ease of doing business in the country; (b) prioritizing corporate and stockholder protection; (c) instilling corporate and civic responsibility; and (d) strengthening the country’s policy and regulatory corporate framework.<sup>1</sup>

Policy makers noted that amendments to the Philippine corporation law were necessary to facilitate ease of doing business in the country, and to promote the development of micro, small, and medium entrepreneurs.<sup>2</sup> They also noted that there was a need to address archaic bottlenecks in the areas of starting a business.<sup>3</sup> The most prominent of these was the presence of the incorporation requirements mandated by Section 10 of the old Corporation Code.<sup>4</sup>

The minimum requirement on the number of incorporators was deemed to be a hindrance in the promotion of the growth of business<sup>5</sup> as it had encouraged the unscrupulous practice of using dummy incorporators in order for entrepreneurs to form a corporation.<sup>6</sup> As a result, the amendments provided for by the passage of the RCC included the formal introduction and recognition of the One Person Corporation (“OPC”) into the Philippine legal framework.

The OPC is the first unipersonal corporate entity in Philippine law of which a private individual may avail. Its introduction is premised on providing entrepreneurs with the option of establishing a unipersonal business

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<sup>1</sup> H. Journal 24, 17th Cong., 3rd Sess. 21 (Oct. 8, 2018).

<sup>2</sup> S. Rpt. 22, 17th Cong., 1st Sess. (2016). Committees on Constitutional Amendments and Revision of Codes and Trade, Commerce and Entrepreneurship.

<sup>3</sup> H. Journal 24, *supra* note 1.

<sup>4</sup> CORP. CODE (1980), §10. *Number and qualifications of incorporators.* — Any number of natural persons not less than five (5) but not more than fifteen (15), all of legal age and a majority of whom are residents of the Philippines, may form a private corporation for any lawful purpose or purposes. Each of the incorporators of a stock corporation must own or be a subscriber to at least one (1) share of the capital stock of the corporation.

<sup>5</sup> H. Journal 24, *supra* note 1.

<sup>6</sup> S. Rpt. 22, *supra* note 2.

organization which has limited liability, unlike a sole proprietorship.<sup>7</sup> By allowing for limited liability, the entrepreneur is given direct control of the growth of his or her business in its initial stages.<sup>8</sup> A further benefit of providing a single person corporate form with limited liability is the limitation of loss on the part of the entrepreneurs which would not preclude them from re-engaging in another business in case of failure.<sup>9</sup>

In this Note, it is advanced that an incidental benefit in the policymakers' introduction of OPCs is the possibility of such being used for estate planning. This argument is hinged upon the presence of succession provisions in the RCC. Specifically, the RCC provides for the transfer of ownership of the OPC from the sole stockholder to the legal heirs.<sup>10</sup> This is not surprising given the common practice in estate planning of using corporate law to effectuate intergenerational transfers of wealth. Using corporation law, an estate planner will be able to consolidate the assets and wealth of a decedent to allow for the proper transfer of properties through the laws of succession.<sup>11</sup>

Estate planning in the Philippines is a balancing act between the decedent's wishes and the rights of heirs, while still complying with the requirements of the law at the same time. Given the common practice of using corporations in estate planning and considering that the existing laws of succession make proper estate planning a herculean task, this Note answers the question of whether an OPC is a viable vehicle for the transmission of wealth from one generation to another. The Note will focus on three areas: first, it will seek to explain the development of the concept of unipersonal corporations; second, it will seek to clarify the supposed advantages offered by the OPC as a corporate vehicle for succession; and third, it will examine whether or not the OPC may be a viable vehicle for succession in light of the rules of succession provided for in the Civil Code of the Philippines.

## **B. The Origins of the One-Man Corporation**

A unipersonal corporation can refer to either (1) a corporation that was incorporated with only one shareholder, or (2) a corporation originally formed by multiple shareholders but thereafter reduced to one shareholder.<sup>12</sup> The

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<sup>7</sup> *Id.*

<sup>8</sup> *Id.*

<sup>9</sup> *Id.*

<sup>10</sup> REV. CORP. CODE, § 132.

<sup>11</sup> SUSANNE KALLS, COMPANY LAW AND THE LAW OF SUCCESSION 6–7 (2015).

<sup>12</sup> Laura Daugherty, *The Sociedad por Acciones Simplificada: Suggestions for Further Reform of Mexico's First Unipersonal Limited Liability Entity*, 27 WASH. INT'L L. J. 743, 744 n. 4 (2018).

development of the concept can be traced to the desire of an individual to combine limited liability with complete dominion over the entity similar to the sole proprietorship.<sup>13</sup> It is by mapping the development of the concept of limited liability that there can be a better understanding of the concept of unipersonal corporations.

Civil law jurisdictions recognized limited liability much earlier than common law jurisdictions.<sup>14</sup> This is evidenced by the adoption of a general enactment of limited liability in the Napoleonic *Code de Commerce* in 1807 which later became the basis of many civil law jurisdictions.<sup>15</sup> Although civil law jurisdictions recognized the existence of limited liability earlier, it was in common law jurisdictions that the development of corporate limited liability first crystalized.

The first general incorporation statutes were passed in England in 1844 to encourage the incorporation of business organizations. In 1855, statutes were passed which provided for general limited liability for corporations.<sup>16</sup> Civil law jurisdictions would do so at a much later time.<sup>17</sup> Yet, for all intents and purposes, the creation and determination of the concept of the one-man corporation has been a judicial one.<sup>18</sup>

The breakthrough moment for the unipersonal corporation was the decision of the House of Lords in the landmark case of *Salomon v. Salomon & Co. Ltd. Co.*<sup>19</sup> The plaintiff in this case was Mr. Aron Salomon, a leather merchant and boot maker who had sold his goods as a sole proprietorship. Under the Companies Act of 1862, Salomon then sold his businesses to Salomon & Co Ltd. (“Salomon & Co.”), a limited liability company which he had incorporated. The company was formed with a nominal capital of 40,000 shares with debentures issued by the company to Mr. Salomon and a certain Mr. Broderip. The incorporators and shareholders of the company consisted of Mr. Salomon who at the time of the liquidation of the company held 20,001 shares issued by the company, while six shares were individually held by his wife and five children. Subsequently, the company experienced financial

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<sup>13</sup> Bernard Cataldo, *Limited Liability with One-Man Companies and Subsidiary Corporations*, 18 LAW & CONTEMP PROBS. 473, 474 (1953).

<sup>14</sup> Dante Figueroa, *Comparative Aspects of Piercing the Corporate Veil in the United States and Latin America*, 50 DUQ. L. REV. 683, 699–700 (2012).

<sup>15</sup> Phillip Blumberg, *Limited Liability and Corporate Groups*, 11 J. CORP. L. 573, 596 (1986).

<sup>16</sup> *Id.* at 578–85.

<sup>17</sup> *Id.* at 574–85, 595–96.

<sup>18</sup> Jules Silk, *One Man Corporations—Scope and Limitations*, 100 U. PA. L. REV. 853, 853 (1952).

<sup>19</sup> [Hereinafter “*Salomon*”], AC 22 (1897).

difficulty and entered liquidation. Following the payment of the debenture obligations of Mr. Broderip, Mr. Salomon claimed ownership over the remaining assets of the company by virtue of his debenture. The House of Lords ruled in favor of Mr. Salomon and ruled that despite Salomon & Co. being owned solely by Mr. Salomon, the latter had a distinct personality from the former.

The House of Lords anchored its analysis of the case on the fact that Mr. Salomon had complied with the requirements laid down by statutes for the incorporation of a company. It opined that as the requisites of the law had been complied with, the application of the doctrine of separate liability was warranted. The House of Lords reasoned that the facts showed that although it was Mr. Salomon who controlled all the shares of the company, no evidence of fraud was adduced which would not lead to the applicability of limited liability. Hence, even if it was a “one-man company,” the law did not preclude it from continuing as a legal corporate body.

*Salomon* thus laid down the fundamental principles regarding the legal recognition of the “one-man” as a valid business organization.<sup>20</sup> The decision upheld that the doctrine of separate personality was still applicable even if the shares of a company was owned or controlled by one shareholder so long as the formal requirements of incorporation were complied with. This implies that the distinct persona of a corporation can be applied to a sole individual as long as the organization was properly and legally incorporated.<sup>21</sup> The second principle laid down was the recognition that there was no wrong committed when an entrepreneur incorporated their business in order to obtain the benefits of limited liability. The decision affirmed that the desire by an entrepreneur to limit their liability and losses should be granted and upheld if the individual complied with the requisites of the law.

The recognition of the “one-man” corporation, however, did not lead to its immediate adoption or acceptance. This is because the premise of a unipersonal corporation is antithetical to the principle that the formation of a corporation was a contract which required more than one person and incorporator.<sup>22</sup> Legislators were also wary of formally recognizing the legality of one-man or unipersonal corporations, as this could possibly lead to the proliferation of the use of dummies and other devious means to create one-man corporations. The potential use of these corporations as means for the

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<sup>20</sup> Cornelius Masten, “*One Man Companies*” and Their Controlling Shareholders, 14 CAN. B. REV. 663 (1936).

<sup>21</sup> G. Van Bergen, *The One-Man Company*, 1 HONG KONG U. J. J. 187, 187 (1926).

<sup>22</sup> Mario Rotondi, *Limited Liability of the Individual Trader: One-Man Company or Commercial Foundation*, 48 TUL. L. REV. 989, 998–1000 (1973-1974).

perpetuation of fraud or deception against creditors and third persons only fueled these apprehensions.<sup>23</sup> This led to strict adherence to the formal requirements of incorporation by many American states. As late as the 1950s, some American states still refused to recognize the legality of a one-man corporation.<sup>24</sup>

These hesitations slowly gave way, however, as many states in the United States slowly began to recognize the incorporation of one-man corporations, or at least began to tolerate their existence through the relaxation of their incorporation statutes.<sup>25</sup> The acceptance gained traction as the benefits of the one-man corporation as a corporate device made its use more prevalent because of the flexibility it gives business owners in the operations of their businesses.<sup>26</sup> The one person corporation was found to be a way to facilitate individual participation in commercial enterprise.<sup>27</sup> As held in the case of *Johnson v. Kinchen*:

Obviously the useful and beneficial role of the corporate concept in the economic and business affairs of the modern day world would be destroyed if the rule of freedom from individual liability for corporate liability did not obtain. The protection of limited liability for venture of investment capital is essential to the efficient operation of a system of free enterprise. Such protection from individual liability encourages and promotes business, commerce, manufacturing and industry which provides employment, creates sales of goods and commodities and adds to the nation's economic and financial growth, stability and prosperity.<sup>28</sup>

This led to the recognition of the one-man corporation as a kind of a closely-held corporation available to entrepreneurs.<sup>29</sup> As a result, the majority

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<sup>23</sup> Cataldo, *supra* note 13, at 475–76.

<sup>24</sup> R. Barry McComic, *Theory of the Corporate Entity and the One-Man Corporation in Louisiana*, 38 TUL. L. REV. 738, 739 (1964).

<sup>25</sup> Mitchell Crusto, *Unconscious Classism: Entity Equality for Sole Proprietors*, 11 U. PA. J. CONST. L. 215, 260–261 (2009).

<sup>26</sup> See Warner Fuller, *The Incorporated Individual: A Study of the One-Man Company*, 51 HARV. L. REV. 1373 (1938).

<sup>27</sup> Rotondi, *supra* note 22, at 989.

<sup>28</sup> *Johnson v. Kinchen*, 160 So. 2d 296 (La. Ct. App. 1964).

<sup>29</sup> Harwell Wells, *The Rise of the Close Corporation and the Making of Corporation Law*, 5 BERKELEY BUS. L. J. 263, 272 (2008).

of American states by the 1990's had accepted or recognized the formation of unipersonal business entities within their jurisdictions.<sup>30</sup>

### C. Unipersonal Corporations in Foreign Jurisdictions

The adoption of the concept of the OPC is part of an ongoing global trend of democratizing and liberalizing incorporation to encourage growth and entrepreneurship. Today, many foreign jurisdictions have recognized and allowed the creation of unipersonal corporations, which are a blend of concepts from both common and civil law.<sup>31</sup>

In the United States, the Model Business Corporation Act, which was revised in 2016, allows for the incorporation of a corporation with only one incorporator and shareholder.<sup>32</sup> Individual states have also adopted the recognition of unipersonal business organizations. Prominent examples are the states of California, New York and Delaware.<sup>33</sup>

In Europe, the first formal adoption of unipersonal business organizations occurred in Liechtenstein in 1925.<sup>34</sup> Over time, more European states slowly began to integrate the concept of unipersonal business organizations into their legal systems. However, the passage of the Twelfth Company Directive issued by the European Economic Community (“EEC”)<sup>35</sup> in 1989 provided a greater impetus for the wide-spread adoption of the concept among European states. The result of its passage was the integration of the concept of a single-shareholder business organization amongst all the legal systems of the EEC's member states. This was then strengthened in 2009 by the passage of Directive 2009/102/EC of the European Parliament of the Council.<sup>36</sup>

Consequently, majority of European states have allowed the incorporation of unipersonal companies or corporations. England's company

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<sup>30</sup> Richard Buxbaum, *Commercial Law - Single Shareholder Company*, 38 AM. J. COMP. L. SUPP. 251, 252-53 (1990).

<sup>31</sup> Daugherty, *supra* note 12, at 743-50.

<sup>32</sup> U.S. Model Business Corporation Act (2016 Revision), §2.01 (2016).

<sup>33</sup> U.S. CA Corp. Code Sec. 200 (2018); U.S. N.Y. Business Corporation Law § 401, U.S. 8 Del. C. c.1 §101

<sup>34</sup> Daugherty, *supra* note 12, at 746-47; Rotondi, *supra* note 22, at 991.

<sup>35</sup> Twelfth Council Company Law Directive 89/667/EEC of 21 December 1989 on single-member private limited-liability companies

<sup>36</sup> Directive 2009/102/EC of the European Parliament and of the Council of 16 September 2009 in the area of company law on single-member private limited liability companies

laws allow for the formation of a single-shareholder company.<sup>37</sup> Despite most civil law jurisdictions still viewing incorporation as a contract, states such as Spain<sup>38</sup> and Italy<sup>39</sup> have accepted the incorporation of a sole person.

The concept of the unipersonal corporation has also been embraced in Latin America. The first Latin American state that recognized the unipersonal corporation was Costa Rica in 1961.<sup>40</sup> This has quickly spread across the region, as there is currently a trend of incorporation of unipersonal corporations with the latest state to introduce it being Mexico.<sup>41</sup>

#### **D. The One Person Corporation in the Philippines**

Under the RCC, an OPC is a corporation with a single stockholder who may be a natural person, trust, or an estate.<sup>42</sup> An OPC may also be formed when a sole stockholder is able to acquire all the shares of stock of an ordinary stock corporation and convert the latter into an OPC.<sup>43</sup> The sole stockholder of an OPC is both the sole director and president of the corporation. As part of the requirements for its formation, the sole stockholder must appoint a treasurer, corporate secretary, and other officers,<sup>44</sup> and must also appoint a nominee or an alternate nominee who will assume management of the corporation upon their death or incapacity.<sup>45</sup>

The OPC is considered a special corporation vested with the powers of a regular corporation. Thus, the OPC must be differentiated from other unipersonal business organizations in the Philippines. Unlike a sole proprietorship, the OPC has a distinct personality from its owner for all purposes.<sup>46</sup> A sole proprietorship, on the other hand, is only deemed to have a separate personality when it is registered with the Department of Trade and Industry, and only then for the purposes of either rehabilitation or liquidation.<sup>47</sup>

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<sup>37</sup> U.K. Companies Act of 2006 (2006), §§ 7, 38.

<sup>38</sup> Spain Ley de Sociedades de Capital (2010), art. 12-17.

<sup>39</sup> Paolo Montalenti, *The New Italian Corporate Law: An Outline*, 1 ECFR 368, 377 (2004).

<sup>40</sup> Daugherty, *supra* note 12, at 747.

<sup>41</sup> *Id.* at 747-49.

<sup>42</sup> REV. CORP. CODE, § 116.

<sup>43</sup> § 131.

<sup>44</sup> § 122.

<sup>45</sup> § 124.

<sup>46</sup> Yao Ka Sin Trading v. Ct. of Appeals, G.R. No. 53820, 209 SCRA 763, 780, June 15, 1992.

<sup>47</sup> Financial Rehabilitation and Insolvency Act of 2010 (2010), § 4(k).



The OPC must also be differentiated from the ecclesiastical corporation sole. The latter is established for the purpose of administering and managing the affairs, property and temporalities of any religious denomination of a church as trustees.<sup>48</sup> Meanwhile, an OPC can engage in any type of business allowed by law and public policy. In the operation of succession, the corporation sole allows for the successor of the current sole holder of the office to assume the place of the sole holder. However, in an OPC, corporate succession only takes place upon the turning over of the shares of the corporation to the heirs or estate of the sole stockholder.<sup>49</sup>

## I. OPC AND SUCCESSION

### A. Intergenerational Estate Planning: Driving Factors for the Transfer of Wealth

Legislators intended that the main beneficiaries from the introduction of the concept of the OPC were small to medium-sized entrepreneurs.<sup>50</sup> They based this rationale on the assumption that having limited liability as an incentive would drive entrepreneurs to formalize and register with the Securities and Exchange Commission (“SEC”) as OPCs, given the primary benefit of encouraging economic growth and the formation of new businesses while minimizing the risks they faced.<sup>51</sup>

Yet for many entrepreneurs, the formation of a business is only the first hurdle. It cannot be denied that many small and medium enterprises are family businesses or sole proprietorships. The reality is that many entrepreneurs have the goal of expanding and growing the business while preparing for the eventual transfer of the business and its assets to the next generation. From this premise stems this Note’s argument that OPCs may be viable tools for succession.

The individual ownership of a substantial portion or the entirety of a business poses a major challenge to any entrepreneur in preparing for the future.<sup>52</sup> The problem is that with much of the individual’s wealth and assets being tied up in the business, the preservation of the business and its assets is vital for any successful intergenerational transfer. This is only exacerbated by

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<sup>48</sup> REV. CORP. CODE, § 108.

<sup>49</sup> §§ 112, 132.

<sup>50</sup> H. Journal 24, *supra* note 1.

<sup>51</sup> S. Rpt. 22, *supra* note 2.

<sup>52</sup> Bertram Tremayne, Jr., *Estate Planning for the Man with a Business*, 1955 WASH. U. L. Q. 40, 40 (1955).

the fact that the death or incapacity of the sole owner or founder of a business organization impacts the ownership and strategic objectives of the organization.<sup>53</sup> Hence, intergenerational transfers regarding a business and its assets between family members involve a myriad of considerations.

It can be argued that there are three factors personal to the business owner in planning the transfer of a business to the heir or heirs. First is the desire to guarantee the continuation of the business while ensuring that the ownership and the control of the business or assets remain with the entrepreneur's family and heirs.<sup>54</sup> Second is the desire to preserve the assets as a source of income for the heirs while minimizing the shrinkage of the value of the property due to transfer taxes and other obligations.<sup>55</sup> The final factor is the need to prevent inter-family jealousy or friction, and to ensure proper business succession.<sup>56</sup>

These considerations are also relevant to an individual who may not be engaged in business. When planning for transfers to their heirs, private individuals are placed in a similar situation of having to dispose of a mass of property and assets to their legal heirs. The legal framework for succession *mortis causa* found in the Civil Code of the Philippines creates this situation, as it is a system of universal succession where the decedent's property, transmissible rights and obligations are acquired *en bloc* by the heirs.<sup>57</sup> As a consequence, there exists the pressing need for a method to properly effectuate the transfer to the heirs upon the decedent's death. The need arises from potential problems that may emerge during the division of the decedent's estate among their heirs.

Compliance with the laws of succession is a major consideration for any person who wishes to prepare for the eventual transfer of wealth to their legal heirs. Succession law, viewed in a broader context, fulfills both economic and social functions. It regulates the transfer of wealth upon the decedent's death and serves as a means to protect the family as a social unit.<sup>58</sup> The core

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<sup>53</sup> Bianca Longo & Andrea Minto, *Intergenerational transfers of entrepreneurial assets. The destiny of the company shares between individualistic aspects and the need for the continuation of the economic initiative*, 2 SUPP. AL. – 1 RICERCHE GIURIDICHE 393, 402 (2013).

<sup>54</sup> Alan Polasky, *Planning for the Disposition of a Substantial Interest in a Closely Held Business*, 44 IOWA L. REV. 83, 128 (1958); Ethan Stroud, *Business Organizations and Estate Planning*, 15 SW. L. J. 542, 544-55 (1961).

<sup>55</sup> Stroud, *supra* note 54, at 544-45.

<sup>56</sup> Polasky, *supra* note 54, at 130.

<sup>57</sup> Jose Reyes, *Reflections on the Reform of Hereditary Succession*, 50 PHIL. L. J. 277, 279 (1975).

<sup>58</sup> Andrea Fusaro, *Company Succession in the Latin Law Tradition Using the Example of the Italian Legal System in COMPANY LAW AND THE LAW OF SUCCESSION* 285-304 (2015).

aim of Philippine succession laws is to uphold the customs and traditions of the Filipino people and to preserve family solidarity.<sup>59</sup> As noted by Justice J.B.L. Reyes, the rules of hereditary succession tend to polarize around inheritance, taxes and escheats.<sup>60</sup>

The foremost challenge in a testamentary disposition of property is the limitations imposed by the system of legitime in testamentary succession. Legitime serves as a limitation upon the freedom enjoyed by the testator in disposing of their property.<sup>61</sup> It reserves a portion of the decedent's estate for their compulsory heirs to secure the latter's needs long after the decedent has died.<sup>62</sup> Such a reservation is enforced to protect the rights of the forced or compulsory heirs who are recognized by law to have a claim in the estate of the decedent.<sup>63</sup>

Intestate succession poses its own unique set of challenges in effecting the transfer of property from the decedents to their legal heirs. In the absence of a will or testament, the inheritance of the decedent's estate will vest with their legitimate and illegitimate relatives, surviving spouse and the State.<sup>64</sup> In cases of intestate succession, the division of the decedent's estate amongst the interested parties is accomplished according to the rules provided for in the Civil Code.<sup>65</sup> The main problem to overcome in intestate succession is whether laws regarding the division of the estate would actually result in the equitable distribution of the estate amongst the heirs.

Notwithstanding these limitations, individuals must also consider the proper management of the assets following their death. Asset management following the death of the decedent must focus on the preservation of the property and ensuring the availability of funds to settle any debts or obligations of the decedent or the estate. This is necessary as it is the estate of the individual that will be held liable for any debts and obligations which survive the death of the decedent.<sup>66</sup> Funds must also be available to settle transfer taxes which are imposed on the right to transfer the property from decedents to their heir or heirs.<sup>67</sup>

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<sup>59</sup> Florida Romero, *Latin Humanism in the Legal System of the Philippines*, 73 PHIL. L. J. 643, 657 (1999).

<sup>60</sup> Reyes, *supra* note 57, at 279.

<sup>61</sup> Romero, *supra* note 59, at 658.

<sup>62</sup> John Boomsri Rodolfo, *Freedom in Death: Expanding the Disposing Power of the Decedent and Providing for a More Rational Sharing of Legitimes*, 51 ATENEO L. J. 544, 545 (2006).

<sup>63</sup> *Id.*

<sup>64</sup> CIVIL CODE, art. 961.

<sup>65</sup> *See* CIVIL CODE, art. 978–1014.

<sup>66</sup> *Alvarez v. Intermediate App. Ct.*, G.R. No. 68053, 185 SCRA 8, 20, May 7, 1990.

<sup>67</sup> TAX CODE, § 84.

Considering these factors, estate planning is of paramount importance to any individual whether engaged in business or not. However, estate planning must be viewed in a broader context as more than just a comprehensive plan of tax reduction.<sup>68</sup> It must be remembered that at its heart, estate planning involves the utilization of the legal devices provided by society for the holding of rights and property during one's life and the transmission of the same following one's death in order to pass such property rights to the desired persons in the desired proportions with the least reduction in the amount of such property.<sup>69</sup> It is here that the OPC's potential as an estate planning tool must be analyzed.

### **B. The Advantages of a Corporate Vehicle**

Senator Franklin Drilon, one of the principal sponsors of the Revised Corporation Code, explained that the OPC is contemplated as a viable corporate vehicle by which a person can manage their estate considering the system of succession in the Philippines.<sup>70</sup> The OPC is a viable tool due to its status as a corporation. Legal scholars have noted that the advantages offered by a corporate form are their perpetual existence, delineation of management and the principle of the transferability of shares.<sup>71</sup> The cumulative effect by the application of corporation law is apparent when the two primary benefits of choosing the corporate form are considered: (1) its advantages in facilitating the transmission of property, and (2) the use of the corporate estate as an estate administration tool following the death of the decedent.

The use of a corporation provides the advantage of creating future interests in assets which do not otherwise lend themselves to the same.<sup>72</sup> It allows for the consolidation of otherwise unrelated assets and properties into one vehicle through which they may be transferred from one generation to the next. Furthermore, incorporation allows for the simplification of the decedent's estate while preserving control over either the business or their personal assets.<sup>73</sup>

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<sup>68</sup> Stroud, *supra* note 54, at 542.

<sup>69</sup> Donald Kelley, *Utility of the Close Corporation in Estate Planning and Administration*, 49 NOTRE DAME L. REV. 334, 336–37 (1973).

<sup>70</sup> S. Journal 56, 17<sup>th</sup> Cong., 1<sup>st</sup> Sess., 882–83 (Jan. 31, 2017).

<sup>71</sup> Polasky, *supra* note 54, at 139.

<sup>72</sup> Kelley, *supra* note 69, at 337.

<sup>73</sup> Ronald Brand, *Estate Planning for the S Corporation Shareholder: Stock Transfers and Investment Tax Credit Recapture*, 45 U. PITT. L. REV. 625, 626 (1984).

With a corporate form, the decedent and estate planner facilitate the transmission of property and assets through the shares of stock of the corporation. This becomes possible as the choice of using a corporate vehicle by the decedent transforms the ownership of their assets and properties from one of direct ownership over property to that of the complex of rights and duties between the shareholder and the corporation.<sup>74</sup> The transformation results in the ownership of the stock of the corporation.<sup>75</sup> These corporate shares are the units of ownership over the property held by the corporation. They are then used to facilitate intergenerational transfer of assets.<sup>76</sup>

As the owner's personal property, a shareholder is at liberty to dispose of these shares in favor of whomsoever he or she pleases, without any other limitation aside from the general provisions of law.<sup>77</sup> By having the ownership of the corporation (and in effect the stockholder's property) represented through shares of stock, transfer of the property is achieved through the transfer of the stock of the OPC to the legal heirs or beneficiaries.

The use of shares benefits the transmission of property significantly in both the short term and long term. In the short term, there are two ways by which stockholder-decedent may avoid matters which may burden their heirs or beneficiaries. First, the use of shares alleviates the need for immediate physical transfer of the properties as the shares of stock will instead be transferred to them upon the death of the decedent.<sup>78</sup> Second, the distinction between corporate property and personal property serves to minimize the property which will be part of the probate proceedings as the consolidation of the rights of ownership into shares means that only the shares will form part of the estate of the decedent.<sup>79</sup>

Using a corporate vehicle allows the decedent to control the distribution of the estate, thus, its long-term benefits. With shares, the decedent may avail of control mechanisms, such as voting control devices or different classifications of shares, to facilitate the transfer of the properties and assets to the target heirs and beneficiaries. This allows for the proper allocation of shares while considering other relevant factors, such as heirs and

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<sup>74</sup> Donald Kelley, *The Farm Corporation as an Estate Planning Device*, 54 NEB. L. REV. 217, 221–22 (1975).

<sup>75</sup> *Id.* at 252–53.

<sup>76</sup> Kelley, *supra* note 69, at 337.

<sup>77</sup> *Fleisher v. Botica Nolasco Co.*, G.R. No. L-23241, 47 Phil. 583, 589 (1925).

<sup>78</sup> Brand, *supra* note 73, at 626–28.

<sup>79</sup> Kelley, *supra* note 69, at 338; Kelley, *supra* note 74, at 259–61.

beneficiaries active in the business, or life of the decedent versus those who may be absent.<sup>80</sup>

More than just a method of facilitating the holding and transfer of property, a corporation is a distinct and separate legal entity from its shareholder.<sup>81</sup> The advantages offered by a corporation as an estate administration tool are predicated on the fundamental principle of corporation law that a corporation is an entity separate and distinct from its stockholders.<sup>82</sup> The result is access to a corporate body which the decedent and their estate planners can use to manage and administer the former's assets and properties.

The perpetual existence of the OPC overcomes the issues presented by the mortality of the decedent. By virtue of its separate personality, the OPC operates with the legal fiction that it is an independent being separate from the stockholder.<sup>83</sup> It possesses its own juridical personality to enter relations and incur its own obligations.<sup>84</sup> This separate personality aids in the eventual administration of the estate's assets as it becomes an independent entity which is able to outlast the lifetime of the decedent. There is also a separation of corporate debt or credit from that of the stockholder which prevents the heirs from incurring any of the corporation's liability until they become owners of the shares of stock.<sup>85</sup>

Incorporation also places the management of corporate properties into the hands of the corporation as corporate assets.<sup>86</sup> Through the application of the doctrine of centralized management, the direct control of these properties is transferred from the stockholder and is instead placed under the control of the board of directors as fiduciary agents.<sup>87</sup> This results in the delineation of management between the stockholder and the corporation as regards the "corporate" property. The delineation of management relieves the sole stockholder of the burden of day-to-day management of the assets as management of the properties can be assigned to employees or officers of the corporation.<sup>88</sup>

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<sup>80</sup> Kelley, *supra* note 74, at 252–255.

<sup>81</sup> *Id.* at 221.

<sup>82</sup> *Concept Builders, Inc. v. Nat'l Lab. Rel. Comm'n*, G.R. No. 108734, 257 SCRA 149, 157, May 29, 1996.

<sup>83</sup> Fuller, *supra* note 26, at 1379.

<sup>84</sup> CIVIL CODE, art. 46.

<sup>85</sup> *Philippine Nat'l Bank v. Hydro Resources Contractors Corp.*, G.R. No. 167530, 693 SCRA 294, 305–06, Mar. 13, 2013.

<sup>86</sup> Kelley, *supra* note 69, at 338.

<sup>87</sup> *Hornilla v. Salunat*, A.C. 5804, 405 SCRA 220, 224, July 1, 2003.

<sup>88</sup> Polasky, *supra* note 54, at 138–39.

An extended benefit of this delineation is the presence of continuity in the management of the assets and property even following the death of the sole stockholder, particularly in instances of the absence of an identifiable heir. Continuity of management and operation is possible in an incorporated estate because the officers, trustees, and employees of the corporation may be called upon to manage the corporation in the interim.<sup>89</sup> This results in the simplification of estate administration, and the attainment of an otherwise unobtainable continuity of business operation is achieved.<sup>90</sup>

### C. The Comparative Advantages of the One Person Corporation

The full utility of the OPC as a vehicle for succession is further demonstrated when comparing it to traditional estate planning tools, such as an ordinary stock corporation and express trusts. An ordinary stock corporation and an OPC provide similar benefits in terms of limited liability and the application of corporation law. However, as compared to an ordinary stock corporation, the OPC's main advantages are its accessibility and the level of control. The OPC is more accessible for individuals due to the less stringent requirements for its incorporation. It also affords the prospective sole stockholder-director a more direct role in the management of the corporation as the OPC merges the benefits of limited liability with the same level of control offered by a sole proprietorship.<sup>91</sup>

Meanwhile, a trust is the legal relationship between one person having an equitable ownership in property and another person owning the legal title to such property, the equitable ownership of the former entitling him to the performance of certain duties and the exercise of certain powers by the latter.<sup>92</sup> Scholars have noted that the versatility of a trust is only limited by the imagination of the lawyers who use them.<sup>93</sup> This is evidenced by the presence of various kinds of trusts with a range of purposes which have been recognized by Philippine law.<sup>94</sup> Such versatility has led to the use of trusts in the Philippines as vehicles for wealth and estate management, administration, and transmission.<sup>95</sup>

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<sup>89</sup> *Id.*

<sup>90</sup> *Id.*

<sup>91</sup> Cataldo, *supra* note 13, at 475; Fuller, *supra* note 26, at 1373–76.

<sup>92</sup> *Morales v. Ct. of Appeals*, G.R. No. 177288, 274 SCRA 282, 298, June 19, 1997.

<sup>93</sup> See Harvey Dychiao, *A Critical Review of the Trust in the Philippines: The Past, Present, and Future*, 52 ATENEO L.J. 46 (2007) for further discussion on the development of the legal concept of Trusts in the Philippines.

<sup>94</sup> *Id.* at 75–96.

<sup>95</sup> *Id.* at 75.

For the purposes of estate planning, a decedent may institute an express trust, which vests the equitable ownership and management of their estate in the hands of a trustee who will administer it for the benefit of the decedent's legal heirs. A trust is a popular tool for estate planning as it may be used in place of a will to direct the disposition and transmission of a decedent's estate through the creative use of the trust agreement.<sup>96</sup>

Scholars have identified two primary kinds of trusts used in estate planning: (1) testamentary trust and (2) *inter vivos* trust.<sup>97</sup> A testamentary trust is commonly set up in wills and takes effect upon the decedent's death.<sup>98</sup> An *inter vivos* trust or "living trust" is created during the life of the decedent.<sup>99</sup> An *inter vivos* trust may be either revocable or irrevocable.<sup>100</sup> Institution of a trust by a private individual provides a multitude of advantages for the purposes of estate planning.

The establishment of a trust provides numerous benefits like those of a corporation. Similar to a corporate form, a trust is able to reduce and consolidate the estate of a decedent, relieve them of the burden of day-to-day management, avoid the institution of probate proceedings involving the property placed in trust, and provide protection and insulation of assets for the benefit of both the decedents and their heirs.<sup>101</sup> Like a corporation, a trust also enables income or benefits to be distributed among heirs but does so without dividing the property.<sup>102</sup>

Aside from these, trusts also possess unique advantages. One advantage is higher levels of privacy are given to the decedent in the disposition of the estate and proceedings.<sup>103</sup> Greater privacy is also derived from the trust's function of avoiding probate as the eventual distribution of the estate will not be subjected to a public proceeding. Trusts are also not subjected to the same

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<sup>96</sup> Thomas B. Hunt, *The Revocable Inter-Vivos Trust in Estate Planning*, 40 J. KAN. B. ASS'N 31, 31 (1971); Timothy Barnhart, *Uses of Trusts in Estate Planning*, 43 ST. LOUIS B. J. 10, 10 (1997).

<sup>97</sup> Dychiao, *supra* note 93, at 63–67; Joseph Berman & Daniel Berman, *Estate Planning*, 57 DICK L. REV. 307, 319–20 (1952); Joseph Berman & Daniel Berman, *A Critical Look at Estate Planning*, 58 DICK L. REV. 232, 241 (1953); Hector De Leon, COMMENTS AND CASES ON PARTNERSHIP, AGENCY AND TRUSTS, 626–27 (2010 ed.).

<sup>98</sup> De Leon, *supra* note 97, at 626.

<sup>99</sup> *Id.* at 627.

<sup>100</sup> Berman & Berman (1953) *supra* note 97, at 241; De Leon, *supra* note 97, at 627.

<sup>101</sup> Dychiao, *supra* note 93, at 75; Berman & Berman (1952), *supra* note 97, at 319.

<sup>102</sup> Glenn Alperstein & William Spinney, *Estate Planning for Lifetime Purposes*, 1963 U. ILL. L.F. 129, 147–53 (1963).

<sup>103</sup> Berman & Berman (1952), *supra* note 97, at 319; Hunt, *supra* note 96, at 33–34.



level of regulation or reportorial requirements in the Philippines as corporations.<sup>104</sup> This provides greater privacy and easier requirements in their formation. Trusts are also relatively easier to dissolve as compared to a corporation.<sup>105</sup> In terms of management and operation, a trust is simpler than a corporation as the trustee is the only party who is directly concerned with the preservation and management of the property.<sup>106</sup> However, despite these advantages, the use of trusts presents four major issues.

The first issue is the relative instability of trust law in the Philippines. There are currently no comprehensive trusts laws and rules in place which govern trusts in the Philippines.<sup>107</sup> Many of the general principles and applications of trusts in the Philippines have been adopted from developments in common law.<sup>108</sup> This has resulted in the adoption of these principles with varying degrees of applicability in our jurisdiction due to the incompatibility of some common law concepts of trust with general principles of civil law.<sup>109</sup> The lack of definitive guidelines and principles is evidenced by the fact that, although the Civil Code of the Philippines provides a general framework for the creation of a trust, more often than not, resort to the courts has been necessary to determine whether or not a trust was created.<sup>110</sup> Such legal uncertainty is mitigated in an OPC, as the estate planner applies concepts of Philippine corporation law which are relatively more defined as compared to trust law.<sup>111</sup>

The second issue is the fact that the decedent and estate planner must properly craft the document instituting the trust to ensure that it can reflect the intentions of the decedent. To reiterate, one of the major benefits of using a trust is the ability to directly administer or dispose of a decedent's estate without the need for a will and additional expenses. However, this requires that the trust agreement or document is crafted in a way which allows the trustee to properly effectuate the disposition of the estate. In addition, the terms of the trust must be broad enough to deal with any eventuality which

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<sup>104</sup> See REV. CORP. CODE, §129 and SEC Mem. Circ. No. 7 (2019), § 13 for reportorial requirements for OPCs.

<sup>105</sup> De Leon, *supra* note 97, at 630.

<sup>106</sup> Hunt, *supra* note 96, at 33.

<sup>107</sup> See Dychiao, *supra* note 93, at 96–106.

<sup>108</sup> *Id.*; see CIVIL CODE, art. 1442.

<sup>109</sup> *Id.*

<sup>110</sup> See *Lorenzo v. Posadas*, 64 Phil. 353, 368–70 (1937); *Sotto v. Teves*, G.R. No. 38018, 86 SCRA 154, 171–73, Oct. 31, 1978; *Ringor v. Ringor*, G.R. No. 147863, 436 SCRA 484, 496–50, Aug. 13, 2004; *Goyanko, Jr. v. United Coconut Planters Bank, Mango Avenue Branch*, G.R. No. 179096, 690 SCRA 79, 86–94, Feb. 6, 2013.

<sup>111</sup> Dychiao, *supra* note 93, at 96–106.

may hinder the disposition and distribution of the estate.<sup>112</sup> This is imperative as a trust does not have a separate legal personality but must act through the trustee, who, in turn, is limited by the trust agreement as regards their powers and duties.<sup>113</sup> The failure to properly plan the trust agreement may deprive the trustee of the necessary powers and flexibility to deal with any unforeseen circumstances which may jeopardize the intent of the decedent, especially if the trust is meant to hold a closely held business.<sup>114</sup>

Unlike a trust, the lack of specific technical details during creation does not hinder the operation of an OPC. The OPC is a more dynamic vehicle in addressing any changes in the decedent's intention or accounting for any unforeseen circumstances which may arise. The separate juridical personality of the OPC grants it powers and attributes which may allow it to adapt quicker to any situation. Administratively, it is also possible to expand the powers of a corporation by amending the OPC's articles of incorporation. The choice of a corporate form allows for the sole stockholder-director to appoint or hire officers, employees, and agents who will be able to act for the decedent independently.

The third issue is the level of control which the decedent retains over the property and assets. The transfer of equitable ownership of the property from the trustor to the trustee is an essential requirement in the creation of a trust.<sup>115</sup> This results in the trustor's loss of active control over the property and assets. Placing the active control of the assets in the hands of the trustee exposes it to potential diminution of value, loss, or destruction which may arise due to the negligence of the trustee. Although there is no direct ownership of the property in an OPC, the decedent, as its sole shareholder and director, still retains control over the property and assets, which are converted into corporate assets.

The final issue is the relative inaccessibility of a trust compared to a corporation from the perspective of an ordinary person. Trusts, as a concept, are relatively inaccessible for non-lawyers because of the lack of set principles defining the concept and the technical complexities involved in executing and implementing them. This makes it difficult for non-lawyers to fully appreciate their full potential.<sup>116</sup> Furthermore, reliance on lawyers and other estate

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<sup>112</sup> See Edward F. Reilly & Keith A. Herman, *Fixing Irrevocable Trust Problems*, 50 ST. LOUIS B. J. 26, 26–28 (2003).

<sup>113</sup> Dychiao, *supra* note 93, at 64.

<sup>114</sup> Peggy Gardner & Morgan Wiener, *Is the Irrevocable Trust Really Irrevocable*, 47 COLO. LAW. 56, 56-57 (2018).

<sup>115</sup> *Morales v. Ct. of Appeals*, 274 SCRA at 297.

<sup>116</sup> Dychiao, *supra* note 93, at 100.

planning professionals increases the administrative costs which must be shouldered by the decedent. It is also worth noting that the operation of trusts services in the Philippines is heavily regulated by the government.<sup>117</sup> This has resulted in many financial and non-financial institutions placing minimum capitalization requirements to individuals who wish to avail of such services. Lastly, the beneficiary must consent to the trust, which makes its feasibility dependent on the will of another party.<sup>118</sup>

The OPC as a tool for estate planning benefits from the fact that there has been a trend towards the liberalization of corporation law which has made the corporation more accessible to the private citizen. Evidence of such liberalization is the absence of minimum capitalization requirements or the need for a minimum number of incorporators for the creation of an OPC.<sup>119</sup> The creation of an OPC is also an act which is solely dependent on the decision of the OPC to incorporate, and not on any other party.<sup>120</sup> These considerations make an OPC relatively more accessible as compared to a trust for estate planning purposes.

### **C. Succession and the One Person Corporation**

Considering the above-mentioned advantages, the use of the OPC as a vehicle for estate planning becomes clearer. A further analysis of the provisions of the law only serves to underscore the desire by lawmakers to make the OPC a tool for succession. This is highlighted by the presence of provisions in the RCC which lay down the process of effecting succession using the OPC, the catalyst of this process being the death of the sole stockholder. The succeeding paragraphs seek to illustrate this process.

W is the owner of different properties and a sole proprietorship. To preserve the value of the business and the properties, W decides to form an OPC named “W Holdings (OPC)” and uses the property of the business and the property he wishes to give to his heirs as the consideration for the shares of stock. W serves as the sole stockholder, director and president of the corporation as laid down by law.<sup>121</sup> In the articles of incorporation, W names Y as his nominee and Z as his alternate nominee.<sup>122</sup> As W is already president, he cannot serve as corporate secretary and instead appoints X as the latter.<sup>123</sup>

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<sup>117</sup> BSP Circ. No. 521-26; GEN. BANKING ACT, §§ 79–82.

<sup>118</sup> CIVIL CODE, art. 1446.

<sup>119</sup> REV. CORP. CODE, §§ 116-17.

<sup>120</sup> § 116.

<sup>121</sup> § 121.

<sup>122</sup> § 118(b).

<sup>123</sup> § 122.

Eventually *W* succumbs to illness and passes away and is survived by his children *A* and *B* and his spouse *C*.

Upon the death of *W*, *X* as the corporate secretary of the OPC is required to immediately inform the nominee (*Y*), or alternate nominee (*Z*) in case of the incapacity of the nominee listed in the articles of incorporation no later than five days from the death of the sole stockholder.<sup>124</sup> The corporate secretary must also give notice to the SEC of the occurrence of the sole stockholder's death and such notice must include the names, residence, addresses, and contact information of all known legal heirs.<sup>125</sup> The corporate secretary must then call the nominee or alternate nominee and the known legal heirs to a meeting to advise the legal heirs regarding, among others, the election of a new director, amendment of the articles of incorporation, and other ancillary and/or consequential matters.<sup>126</sup>

*Y*, as the nominee, or *Z*, as the alternate nominee, is then tasked to sit as the director of the OPC to manage its affairs until the legal heirs of the single stockholder have been lawfully determined, and the heirs have designated one of them or have agreed that the estate shall be the single stockholder of the OPC.<sup>127</sup> The term of the nominee or alternate nominee's management is to continue until the determination by the legal heirs of who will take the place of the deceased sole stockholder as director.<sup>128</sup>

Succession of the designated heir to the status of sole stockholder is done through the transfer of the shares from the sole stockholder-decedent to the legal heirs or estate of the former.<sup>129</sup> The transfer is initiated when the heir presents either an affidavit of heirship or self-adjudication by a sole heir, or any other legal document declaring the legal heirs of the single stockholder.<sup>130</sup> The transfer of the shares must then be done within seven (7) days from receipt of the aforementioned document.<sup>131</sup> Following the transfer of the shares, *A*, *B* and *C*, as the legal heirs, are given sixty days to decide to either wind up or dissolve the OPC or convert it into an ordinary stock corporation.<sup>132</sup> In both instances, the heirs can claim ownership of what is

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<sup>124</sup> §§ 118, 123(a); SEC Mem. Circ. No. 7 (2019), § 7.

<sup>125</sup> REV. CORP. CODE, §123(c).

<sup>126</sup> § 123(d).

<sup>127</sup> § 123(d).

<sup>128</sup> SEC Mem. Circ. No. 7 (2019), §12.

<sup>129</sup> REV. CORP. CODE, §124.

<sup>130</sup> § 132.

<sup>131</sup> § 132.

<sup>132</sup> § 132.

due to them by dividing the corporate property or the shares to match the intended disposition by the decedent.

This example illustrates the advantages of using the OPC in ensuring a successful transfer from the decedent to the legal heirs. The consolidation of the business assets and property into the OPC simplifies the inventorying of assets and lessens the amount of personal property which must be inventoried. This would be advantageous in both types of succession. The actual transfer of the business assets is further simplified as the only assets that need to be transferred are the sole stockholder-decedent's shares in the OPC to their legal heirs. There is also no loss of continuity as the assumption of the nominee or alternate nominee of the role of sole director and president of the corporation mitigates any potential losses and damage the properties or assets may face. Finally, the legal heirs can protect their interests by being given the option to dissolve the corporation or to convert it to a regular stock corporation.

However, a further review of the process provided for in the RCC raises some issues regarding the viability of the OPC as an estate planning tool. The issues are especially problematic when an OPC is used as a vehicle to transfer a substantial portion or the entirety of a decedent's estate. The problems are rooted in a conflict between the RCC and the existing laws of succession.

## **II. ADDRESSING ISSUES IN OPC TRANSFERS**

Potential conflict between the provisions of the RCC and the rules of succession in the Civil Code arises from the determination of what is the actual asset that may be transmitted from one generation to the next, and the definitive rules guiding such transmission. The author argues that the following issues must be addressed in order to determine the viability of the OPC as a vehicle for succession: (1) the determination of what in the incorporated estate constitutes the personal property of the sole stockholder-decedent as distinguished from corporate property, (2) the determination of the applicable rules on the division of the OPC in the event of multiple heirs, and (3) the determination of the role of the nominee or alternate nominee in the transfer process.

### **A. Drawing The Line Between Personal and Corporate Property**

The need to determine the proper object of succession in using the OPC as an estate planning tool stems from the fact that the sole stockholder

has two roles simultaneously.<sup>133</sup> The sole stockholder is both the stockholder and an incorporated corporation.<sup>134</sup> It is only due to the legal fiction that the OPC and the sole stockholder are treated as separate beings. The separation extends as well to the personal property of the sole stockholder and the corporation.<sup>135</sup>

The merging of these two separate identities makes the comingling of the interests, rights, and obligations of the sole stockholder and those of the corporation highly likely.<sup>136</sup> This may lead to instances when the sole stockholder of an OPC treats the corporation and its assets as his or her personal property.<sup>137</sup> Thus, an issue arises on whether an OPC and its assets are the personal property of the sole stockholder which may be transmitted directly to his or her heirs.

The RCC provisions and the relevant SEC Memorandum Circulars make it explicitly clear that the subject of the transfer from the sole stockholder of an OPC are the shares of stock in the corporation.<sup>138</sup> It must be reiterated that the consequence of choosing to incorporate as an OPC results in the transfer of the sole stockholder's ownership over his or her property and assets to the corporation as the consideration for the shares of the OPC. Hence, the only real personal property in the hands of the sole stockholder-decedents are the shares of stock in the OPC.<sup>139</sup>

Philippine jurisprudence is clear that the mere ownership of shares of stock in a corporation does not equate to direct ownership of the corporation or its property.<sup>140</sup> Shares of stock only represent a proportionate or aliquot interest in the property of the corporation; it does not vest the owner thereof with any legal right or title to any of the property, the shareholders interest in the corporate property being equitable or beneficial in nature.<sup>141</sup> Any interest by the shareholder is purely inchoate or a sheer expectancy of a right in the

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<sup>133</sup> Cataldo, *supra* note 13, at 482; Fuller, *supra* note 26, at 1376–77.

<sup>134</sup> Fuller, *supra* note 26, at 1376–77.

<sup>135</sup> Cataldo, *supra* note 13, at 475–77.

<sup>136</sup> See Fuller, *supra* note 26, at 1376–97.

<sup>137</sup> *Id.* at 1389–94.

<sup>138</sup> See REV. CORP. CODE, § 132, SEC Mem. Circ. No.7 (2019), § 12.; SEC Mem. Circ. No. 27 (2020).

<sup>139</sup> REV. CORP. CODE, § 62.

<sup>140</sup> See *Magsaysay-Labrador v. Ct. of Appeals*, G.R. No. 58168, 180 SCRA 266, Dec. 19, 1989; *Boyer-Roxas v. Ct. of Appeals*, G.R. No. 100866, 211 SCRA 470, July 14, 1992, *citing* *Stockholders of F. Guanzon and Sons, Inc. v. Reg. of Deeds of Manila*, G.R. No. 18216, 6 SCRA 373, Oct. 30, 1962; *Mobilia Prod., Inc. v. Umezawa*, G.R. No. 149357, 452 SCRA 736, Mar. 4, 2005.

<sup>141</sup> *Magsaysay-Labrador v. Ct. of Appeals*, 180 SCRA at 271–72.

management.<sup>142</sup> The reality then is that a shareholder is in no legal sense the owner of corporate property as it is owned by the corporation, which is a distinct legal person.<sup>143</sup> This inchoate nature also extends to the rights of any successor of the shareholder.<sup>144</sup> This finds basis in the trust fund doctrine which states that the capital stock, properties, and other assets of the corporation are property held in trust by the corporation on behalf of the stockholders. It is held in trust to service the corporation's debts and obligations, with the shareholder only obtaining actual rights over remaining corporate property following the dissolution of the corporation.<sup>145</sup>

Thus, in both testate and intestate succession, the only permissible object of succession must be the shares of stock in the OPC. American jurisprudence affirms this view, with the general rule being that the ownership of all the shares of stock in a corporation does not equate to direct ownership of the corporation's property or assets by the sole shareholder.<sup>146</sup> However, there have been instances where American courts have upheld the validity of a testamentary disposition of corporate property by a sole stockholder decedent, the majority view being that a testamentary disposition or bequest made by a sole stockholder may be upheld to ensure an equitable interpretation and execution of the decedent's will.<sup>147</sup> A prominent example is the case of *In Re Bush's Estate*.<sup>148</sup>

In the aforementioned case, the decedent was the sole shareholder of a corporation which owned shares of stock in another corporation. The decedent then bequeathed these shares to a legatee. It was alleged that the bequest was invalid as the property in question was a corporate property. The court applied the doctrine of piercing the corporate veil and disregarded the separate personality of the corporation citing that as a matter of justice and equity, the disposition had to be upheld. It also affirmed that the disposition was valid as no corporate creditors would be prejudiced by the sustainment of the validity of the disposition.

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<sup>142</sup> *Id.*

<sup>143</sup> *Philippine Nat'l Bank v. Aznar*, G.R. No. 171805, 649 SCRA 214, 231–32, May 30, 2011.

<sup>144</sup> *See* *Mayor v. Tiu*, G.R. No. 203770, 810 SCRA 256, Nov. 23, 2016.

<sup>145</sup> *Lu v. Lu Ym, Sr.*, G.R. No. 153690, 643 SCRA 23, 80, Feb. 15, 2011.

<sup>146</sup> *See* 18A AM. JUR. 2D CORPORATIONS § 623; *Annotation, Validity, Construction and Effect of Bequest of Property Owned by a Corporation in Which the Testator has Majority Interest*, 78 A.L.R. 3D 968 (1977).

<sup>147</sup> James Walsh, Comment, *Masline v. Buckley*, 6 CONN. PROB. L. J. 367, 368-70 (1992).

<sup>148</sup> 124 Misc. 674, 209 N.Y.S 776 (N.Y. Sur. Ct. 1925).

Analyses of *In Re Bush's Estate* and other similar cases<sup>149</sup> have noted that the main consideration of American courts is the presence of corporate creditors who would be prejudiced by such dispositions, and whether or not such dispositions will affect the liquidating value of the remaining corporate assets.<sup>150</sup> It must also be noted that the majority view in American jurisprudence seems to accept that the need to uphold a decedent's testamentary disposition is a valid reason to pierce the corporate veil and disregard the separate personality of the corporation and sole stockholder.<sup>151</sup>

The potential application of how American courts view the direct disposition of corporate property in Philippine jurisdiction may not be possible for a variety of reasons. First, the only property which the sole stockholder may dispose of is his or her shares of stock in the OPC. Second, the operation of the trust fund doctrine bars a direct testamentary disposition of corporate property as such instances may still impair corporate capital and prejudice future corporate creditors if the OPC continues or is converted into an ordinary stock corporation. Third, there is still no definitive jurisprudence which states the position of the Philippine Supreme Court on this matter.

It also remains unclear whether Philippine courts would consider the need to uphold such testamentary dispositions as a valid reason to disregard the separate personality of the sole stockholder and the OPC. It is a well-settled doctrine that mere ownership of all the shares of all stock of a corporation by a single stockholder is not a sufficient ground to justify disregarding the doctrine of separate personality.<sup>152</sup>

The remedy of piercing the corporate veil is strictly applied and may only be available in certain instances: (a) when the corporate fiction is used as a vehicle for the evasion of an existing obligation; (b) in cases of fraud or when the corporate entity is used to justify a wrong, protect fraud, or defend a crime; or (c) in alter ego cases, where a corporation is merely a farce since it is a mere alter ego or business conduit of a person, or where the corporation is so organized and controlled and its affairs are so conducted as to make it merely an instrumentality, agency, conduit or adjunct of another

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<sup>149</sup> See *In re Cartledge's Estate*, 118 Misc. 131, 192 N.Y.S 838 (N.Y. Sur. Ct. 1922); *In re Freidman*, 177 A.D. 755, 164 N.Y.S 892 (N.Y. App. Div. 1917); *In re. Koffend*, 15 N.W.2d 590 (Minn. 1944); *In re Greenfield Estate* 321 A.2d 922 (Pa. 1974).

<sup>150</sup> J. Walsh, *supra* note 147.

<sup>151</sup> Fuller, *supra* note 26, at 1399–1401.

<sup>152</sup> *Francisco v. Mejia*, G.R. No. 141617, 362 SCRA 738, 753, Aug. 14, 2001.



corporation.<sup>153</sup> The need to uphold a testamentary disposition does not seem to fall squarely under any of these circumstances.

The applicability of the doctrine of piercing the corporate veil of OPCs may also put into question the practicality of incorporation. The comingling of the interest of the sole stockholders with that of the corporation makes them susceptible to incurring personal liability for using corporate funds for personal matters. Section 130 of the RCC explicitly states that where the single stockholder cannot prove that the property of the One Person Corporation is independent of the stockholder's personal property, the stockholder shall be jointly and severally liable for the debts and other liabilities of the OPC.<sup>154</sup>

Thus, it is possible that the sole stockholder will not be able to shield both the corporate property and the shares of stock from corporate creditors. This puts into question whether it would be beneficial to incorporate as there is no guarantee that the property and asset can be preserved until eventual transfer to the legal heirs. The liabilities incurred by the sole stockholder may even burden the legal heirs. It is possible that the piercing of the corporate veil may lead to creditors of the corporation going after the shares of the OPC. It is also possible that the conversion of an OPC into a regular stock corporation will expose the heirs to these liabilities as conversion does not relieve the new corporation from the outstanding liabilities of the original OPC.<sup>155</sup>

## **B. The OPC Post-Death: Dividing the OPC**

The second issue that must be clarified is the method by which the OPC can be used to transfer the assets of the decedent to the legal heirs. This is of particular importance in instances when majority of the decedent's estate is composed of the shares of the OPC. Hence, a determination must be made as to which rules will govern the transfer of the shares following the death of the latter, and how to divide the shares amongst the heir or heirs.

The laws which govern the transfer of the shares are the provisions of the RCC and the relevant SEC Memorandum Circulars. Applying the rules of statutory construction, *lex specialis derogate general*, in instances when there are two similar enactments, it is the special law which will be controlling over a general statute.<sup>156</sup>

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<sup>153</sup> Philippine Nat'l Bank v. Hydro Resources Contractors Corp., 693 SCRA at 307, *citing* Sarona v. Nat'l Lab. Rel'n Comm'n, G.R. No. 185280, 663 SCRA 394, 417, Jan. 18, 2012.

<sup>154</sup> REV. CORP. CODE, § 130.

<sup>155</sup> § 132.

<sup>156</sup> Barcelote v. Republic, G.R. No. 222095, 834 SCRA 564, 578 (2017).

In this regard, the provisions of the RCC fulfill this role. Legal scholars note that the situations involving the eventual disposition of an OPC may fall into one of two scenarios.<sup>157</sup> The first involves instances when the OPC is used as a convenience with the financial operations of the sole shareholder which will be dissolved after the death of the sole stockholder. The second scenario involves instances when the intent of the decedent is the continuation of the OPC by his or her heirs.

The procedure provided for in the RCC clearly contemplates these two different scenarios. First, the procedure identifies that the ownership of the shares of stock in the OPC should eventually be transmitted to the legal heirs of the sole stockholder-decedent. Second, the procedure gives the legal heirs the options of either winding-up and dissolving the OPC or continuing its existence as is or by converting it into an ordinary stock corporation.<sup>158</sup>

Yet, neither the RCC nor SEC Memorandum Circulars have laid down definitive guidelines for the eventual division of the shares amongst the heirs. As the special law is silent on a matter which is still clearly related to succession, the provisions of the Civil Code on succession must apply suppletorily. This position is supported by the deliberations in the drafting of the RCC in which Senator Drilon explicitly stated that the existing laws of succession would apply in the succession of the legal heirs to the OPC.<sup>159</sup>

Legislators, however, did not foresee that the suppletory application of the Civil Code could potentially conflict with the supposed advantages of choosing the OPC as a vehicle for succession. One of the main advantages offered by the OPC is predicated on the transferability of shares, the idea being premised on the simple notion that the shares owned by the decedent simply pass on to the legal heirs.

The effect of applying the rules of hereditary succession necessitates that the transfer and division of shares must comply with the rules of legitime or the division of the estate in case of intestate succession. These rules run counter to the idea of using the shares of stock to properly concentrate the shares in the intended legal heir.<sup>160</sup> This is because a system of forced division of the corporation's shares limits the number of shares which may be inherited

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<sup>157</sup> Fuller, *supra* note 26, at 1398.

<sup>158</sup> REV. CORP. CODE, § 132.

<sup>159</sup> S. Journal 56, *supra* note 70.

<sup>160</sup> Martin Schauer, *Intergenerational Transfer of Wealth from A Comparative Perspective. Different solutions to a complex problem*, 2013 RICERCHE GIURIDICHE 2 SUC AL. – 1 402.

by an heir.<sup>161</sup> It must also be remembered that as the Philippines follows a system of universal succession. This means that all legal heirs have a right to the estate upon the opening of succession. This complicates the division of the shares of the OPC as the procedure provided for in the RCC assumes that the nominee and heirs have an idea of how to divide the shares. The consequences of these factors result in the following issues.

First, as each legal heir has a claim to the shares of stock in the OPC, it is difficult to determine which of them should be chosen to succeed as the sole director and president of the OPC, as such an election may possibly be an infringement upon the compulsory shares of the other heirs. It is untenable to presume that the selection of one heir considering the acts of other heirs is a renunciation or waiver of their rights to the shares of stock in the OPC. Second, there is a need to determine to what extent the shares of the OPC the heir will inherit, and whether it complies with the legitime or the compulsory share from intestate succession. These issues illustrate that the process in the RCC did not explicitly clarify what document will govern not just the transfer of the shares, but also in the eventual division.

This Note argues that to overcome these limitations and use the OPC as a viable tool for succession, the solution is the conversion of the OPC upon the death of the decedent. It has already been discussed that the continuation of the OPC as a corporation may not prevail against compulsory shares.<sup>162</sup> Hence, the conversion of the OPC into a regular stock corporation allows the decedent to maximize the OPC as a vehicle for succession.

Conversion into a regular stock corporation also overcomes some of the technical hurdles of succession as the OPC itself can be used as a form of disposition that guides the transfer and division of the OPC in conjunction with the documents required by the provisions of the RCC in transferring and eventually dividing the OPC. This is possible as the decedents and their estate planners can use the articles of incorporation and the by-laws of the OPC to place restrictions on the transfer of the shares of stock to the heirs of their heirs. As a form of closely-held corporation, it is possible to use these two documents as a way to effect the transfer of shares to an intended heir independent of a will.

Using the earlier example of W and “W Holdings (OPC)”, W during the incorporation of the OPC can place in his articles of incorporation that following his death, the OPC will be immediately converted into an ordinary

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<sup>161</sup> *Id.*

<sup>162</sup> *Id.*

stock corporation. This would immediately ensure that the division required by law for legitime or compulsory shares in intestate succession is complied with as the division of the corporation is already contemplated.

The use of the articles of incorporation and the by-laws of an OPC can also be used to direct the eventual transfer of the shares to the intended heir following the forced conversion of the OPC into an ordinary stock corporation. Conditions and restrictions can also be imposed such that each specific heir is the only person entitled to inherit the stock. In the illustration, W can state in the articles of incorporation that a certain number of shares are determined by the relation of the heir with the original sole stockholder. Through this forced conversion, the rights of the heirs are not impaired and the intent of the decedent, if any, is respected.

### **C. Determining the Extent of Nominee or Alternate Nominee's Participation**

The RCC highlights the importance of the role of the nominee, or his or her alternate in any intergenerational transfer conducted through OPCs. The nominee, or in his or her absence, the alternate, acts as the sole director and president of the OPC until the decedent's heirs settle issues pertaining to the decedent's estate.<sup>163</sup> They are also tasked to transfer the shares of the OPC to the selected legal heir chosen to replace the decedent. In this Note, it is argued that the relationship of the sole stockholder and the nominee or alternate nominee is an implied constructive trust as it arises by operation of the RCC.

The Civil Code defines an implied trust as one formed by the operation of law.<sup>164</sup> They are deducible from the nature of the transaction as matters of intent or independently of the particular intention of the parties as being superinduced on the transaction by operation of law basically by reason of equity.<sup>165</sup> A constructive trust is one that arises by implication of law and always presumed to have been contemplated by the parties, or a resulting trust which is based on the equitable doctrine that it is the more valuable consideration than the legal title that determines the equitable interest in property.<sup>166</sup>

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<sup>163</sup> REV. CORP. CODE, § 124.

<sup>164</sup> CIVIL CODE, § 1442.

<sup>165</sup> *Heirs of Lorenzo Yap v. Ct. of Appeals*, G.R. No. 133047, 312 SCRA 603, 608, Aug. 17, 1999.

<sup>166</sup> *Id.*

In this instance, the operative law which creates the constructive trust is the RCC. This is apparent as the appointments of a nominee and alternate nominee are *sine qua non* requirements laid down by the RCC for the incorporation of an OPC. They are appointed in contemplation of the inevitable death of the sole stockholder as shown by the fact that their duty to manage the corporation is predicated on the latter's death.<sup>167</sup>

Their obligations as trustee are two-fold. First, they are to serve as the temporary sole stockholder and director of the OPC until the appointment of the legal heir who will replace the original sole stockholder. Second, they are given the duty of transferring the shares to the legal heirs of the sole stockholder upon the presentation of documents which prove the identity of the latter. These duties are done to satisfy the demands of justice as they merely effectuate the objective of the law to have the ownership of the shares of the OPC arrive at the hands of the sole stockholder's legal heirs.

### CONCLUSION

The use of OPCs as a vehicle for succession is predicated on the application of corporate law doctrines to effect the transfer of the decedent's property and assets to his or her heirs. The pertinent doctrines are the doctrines of separate personality, limited liability, and the transferability of shares. The application of these concepts cumulatively results in the advantages of using the OPC to facilitate the transmission of the property and the management of the estate following the death of the decedent.

It is proven, however, that these advantages are limited by the existing system of succession in the Philippines.

First, it is shown that the transformation of direct ownership over the property into shares does not necessarily ensure the successful and equitable transfer to the proper heir. The doctrine of limited liability does not protect the interest of the sole stockholder and the heirs due to the implications of the former comingling the interests and obligations. The need to comply with compulsory shares also precludes any disposition of the shares in a manner which properly concentrates the assets into the proper heir.

Second, the process provided for in the transfer of ownership of the OPC ignores the reality of competing interests amongst heirs in the partition and division of the estate of the decedent. It is not unlikely that these

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<sup>167</sup> REV. CORP. CODE, § 124.

competing interests may render the application of the rules of transferring the shares of the OPC impossible to apply or may even make it an inequitable or illegal transfer. This is most problematic for the nominee or alternate nominee who must transfer the shares to the heir “chosen” to represent the others when the former assumes the role as sole stockholder and director of the OPC.<sup>168</sup>

It is also noted that there are additional factors which must be considered, including the impact of the reportorial requirements of an OPC in the actual maintenance and operation of the corporation.<sup>169</sup> The need to comply with these requirements may serve to further undermine the autonomy and flexibility of using the OPC as a vehicle for succession by imposing additional expenses and obligations. Another factor to consider is, whether the supposed tax benefits offered by incorporation are practical given that amendments to the National Internal Revenue Code have removed the graduated taxation rate for estate tax and now impose a single rate of six percent. An additional area for study involving the efficacy of using a corporate form must also contend with the presence of additional taxes which are imposed in the transfer of the shares, the dissolution of the corporation and other transactions related to the transfer of the ownership of the OPC.

In conclusion, the OPC as a vehicle for succession is viable but limited by the existing laws of succession. Although theoretically sound, the reality of the situation puts into question whether it lives up to its goal of being a vehicle for succession as envisioned by lawmakers. Its potential may only be realized if there are major revisions or amendments to the rules of succession which would allow for the theoretical advantages to be applicable more smoothly.

A possible amendment which may be introduced is the reduction or adjustment in the compulsory shares which are reserved for the decedent’s legal heirs. The existing system of compulsory shares, especially in cases of testamentary succession, is based on the assumption that the decedent is able to leave an equal share of the estate for all heirs, and that the decedent wishes for all their heirs to have equal shares.<sup>170</sup> The reality, however, is that the existing system of compulsory shares ignores the actual state of a decedent’s estate as well as the unique needs of a decedent’s legal heirs.<sup>171</sup> It may even result in inequality which would run counter to the very purposes the system

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<sup>168</sup> § 132; SEC Mem. Circ. No. 7 (2019), § 12.

<sup>169</sup> SEC Mem. Circ. No. 7 (2019), § 13.

<sup>170</sup> Rodolfo, *supra* note 62, at 584–87.

<sup>171</sup> *Id.*

of compulsory shares was instituted. An adjustment and reduction of the compulsory shares would allow for a more efficient use of OPCs for estate planning. Enacting such reforms would relieve the burden imposed by the current system of compulsory shares on estate planners in the distribution of the shares of the OPC among a decedent's heirs while respecting their wishes as to who gets what, and to what extent.

An alternative to a full-blown adjustment of the system of compulsory shares would be a limited introduction of inheritance contracts in this jurisdiction. Under current Philippine law, there is a prohibition on contracts regarding future inheritance.<sup>172</sup> This prohibition is common among many civil law jurisdictions as it defeats the principle of equality of heirs and is grounded on the practical fear that the creation of such contracts would prove dangerous to the decedent's life.<sup>173</sup> However, legal scholars have abandoned such apprehensions and now argue for the removal of such prohibitions.<sup>174</sup>

In essence, an inheritance contract is an agreement where one contracting party appoints the other to be his or her heir, or they mutually appoint each other as heirs, or appoint as such a third party, with or without compensation.<sup>175</sup> The adoption of inheritance contracts was greatly accelerated by the recognition of its potential in effecting intergenerational transfers of family businesses and shares in family owned corporations.<sup>176</sup> This has been adopted by many civil law jurisdictions in Europe with varying degrees of flexibility and applicability.<sup>177</sup> In light of the public policies and principles underlying the system of succession of the Philippines, a feasible inheritance contract model which Philippine legislators may pattern such contracts is the Italian *Patto Di Famiglia*.<sup>178</sup>

The *Patto di Famiglia* (model of family contract or family agreement) is a highly restrictive form of inheritance contract or agreement.<sup>179</sup> It is a contract that allows an entrepreneur or shareholder to partially or wholly

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<sup>172</sup> CIVIL CODE, art. 1347.

<sup>173</sup> Dragica Zivojinovic & Tamara Durdic-Milosevic, *Inheritance Contract and Its Substitutes in European and Serbian Law*, 17 REV. EUR. L. 69, 71 (2015); Reyes, *supra* note 57, at 281–82.

<sup>174</sup> Reyes, *supra* note 57, at 281–82.

<sup>175</sup> Zivojinovic, *supra* note 173, at 73–74.

<sup>176</sup> 94/1069/EC: Commission Recommendation of 7 December 1994 on the transfer of small and medium-sized enterprises, art. 5.

<sup>177</sup> Zivojinovic, *supra* note 173, at 73–74.

<sup>178</sup> *Id.*; Holger Fleischer, *Family Firms and Family Constitutions: A Legal Primer*, 15 EUR. COMPANY L. 11, 13–14 (2018).

<sup>179</sup> Fleischer, *supra* note 178, at 13–14; Zivojinovic, *supra* note 173, at 77–80; Fusaro, *supra* note 57, at 296–298.

transfer the business to one or more descendants.<sup>180</sup> Italian law requires that all forced heirs and the spouse of the entrepreneur must participate and consent to the creation of the agreement.<sup>181</sup> It is an exception from the general prohibition on contracts of future inheritance and is only applicable to the disposition of the family business or shares therein. The effect of the institution of a *Patto di Famiglia* is the continuity of the family business through the lifelong regulation of relations between potential successors of a company, the ultimate objective being the protection of general economic interest.<sup>182</sup> Similar types of agreements or contracts have been adopted in Spain which have proven useful in overcoming the hindrances of Spanish succession law.<sup>183</sup>

It is worth pondering whether or not the introduction of a similar contract in the Philippines would alleviate problems in succession. This form of inheritance contract arguably limits possibility of abuse while simultaneously granting a decedent the necessary flexibility to use their OPC to its full potential for estate planning. The OPC as an estate planning tool would benefit from the use of such agreements as the decedent will be able to properly plan the transfer of the shares without having to do so through a will, or have such agreements invalidated as being a void contract. These are only some possible revisions or amendments which may be made to the existing laws of succession. Others should also be explored in order to realize the full potential of the OPC as an estate planning tool.

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<sup>180</sup> Fleischer, *supra* note 178, at 13–14; Fusaro, *supra* note 58, at 296–98.

<sup>181</sup> Zivojinovic, *supra* note 173, at 77–80; Fusaro, *supra* note 58, at 296–98.

<sup>182</sup> *Id.* at 80.

<sup>183</sup> Fleischer, *supra* note 178, at 13; Jaume Tarabal Bosch, *Will-Substitutes in the U.S. and in Spain*, 103 IOWA L. REV 2293, 2303–15 (2018).