ASSESSMENT OF THE INITIAL PUBLIC OFFERING*

I. INTRODUCTION

In the early nineties, Initial Public Offerings (IPOs) were considered to be the hottest items in the stock market, enticing many firms to consider this scheme as a means to raise their much needed capital to finance business expansions or to jumpstart new projects. Through the years, however, IPOs seem to have lost their appeal on both the issuing corporations and investors. The number of firms going public as well as the total capital raised from such IPOs has not regained the robust numbers they showed at the time when IPOs were still very attractive to the investing public. Players in the domestic capital market identify the IPO tax as one of the major factors behind the lukewarm interest of going public because said tax allegedly increases the cost of IPO transactions.

The Philippines is the only country in Asia that imposes an IPO tax on shares of stock sold, bartered or exchanged or otherwise disposed in the local stock exchange. It is also noted that the Philippines has a higher transaction cost for transfer of shares compared to Hong Kong, Thailand and Singapore.[1]

This paper seeks to examine the performance of the IPO tax and its impact on the decision of companies to go public.

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[1] Iris C. Gonzales, “Scrapping of IPO Taxes Urged”, The Philippine Star, July 10, 2007, page B1.

II. BACKGROUND INFORMATION

A. Concept of IPO

An IPO refers to stock offering made for the first time in the local stock market.[2] Its objective is to seek a public market for the stocks of a company that wishes to raise capital, thus encouraging public participation in stock transactions. The IPO is the common method for a company to become "listed" in the Philippine Stock Exchange (PSE), hence, transforming privately-closed company to a publicly-held and traded company whereby the ownership of shares in a company is distributed for the benefit of the investors and the domestic market as well.

The primary purpose of the IPO is to increase capital in a cost-effective way because it allows business expansion without increasing borrowings or draining the company′s cash reserves. Other reasons for undertaking an IPO would be to improve the company's profits and increase the potential for mergers or acquisitions. The last but not the least reason for going public is to comply with the requirements of some laws for some sectors (e.g., BOI-registered enterprises, oil-refinery businesses, and telecommunication companies).

B. Laws on the IPO Tax

The IPO taxation started in 1994, with the enactment of Republic Act (RA) No. 7717.[3] It was later amended by RA No. 8424[4] otherwise known as the "Tax Reform Act of 1997".

As provided in said RA, the IPO tax is based on the gross selling price or gross value in money of the shares of stock sold, bartered, exchanged or otherwise disposed in accordance with the proportion of said shares of stock to the total outstanding shares of stock after its listing in the local stock exchange. Taxpayers who are liable to the IPO tax are the issuing corporations in primary offerings and the sellers in case of secondary offerings.[5] In the case of primary offering, the issuing corporation is liable to file the tax return and pay the tax within 30 days from

[2] BIR Revenue Regulation 3-95, February 7, 1995.

[3] "An Act Imposing a Tax on The Sale, Barter or Exchange of Shares of Stock Listed and Traded Through The Local Stock Exchange or Through Initial Public Offering, Amending For The Purpose The National Internal Revenue Code, As Amended, By Inserting a New Section and Repealing Certain Subsections Thereof," approved on May 5, 1994 and effective on May 28, 1994.

[4] "An Act Amending the National Internal Revenue Code, As Amended, and For Other Purposes", approved on December 11, 1997 and effective on January 1, 1998.

[5] The PSE defines primary offering as the original sale made to the investing public by the applicant company of its own securities (i.e. primary shares) and secondary offering as an offer for sale made to the investing public by the existing shareholders of their securities which are already issued (i.e. secondary shares).

the date of listing of the shares of stock in the local stock exchange. In the case of secondary offering[6], the seller is the one primarily liable to the IPO tax but the filing of the corresponding return is the duty of the stockbroker. The stockbroker collects the tax from the proceeds of the sale and remits the same to the Bureau of Internal Revenue (BIR) within five (5) banking days from the date of collection thereof.[7]

The table below shows the changes introduced by RA No. 8424 in the IPO tax base.

Table 1. LAWS ON THE IPO TAX

Law	Tax Base	Tax Rate	Effectivity Date
RA No. 7717	Gross selling price or gross value in money of shares of stocks sold, bartered, exchanged or otherwise disposed in accordance with the proportion of stocks sold, bartered or exchanged or after listing in the stock exchange. • 33⅓% or below • Over 33⅓% but below 50% • Over 50%	 4% 2% 1%	Approved: May 5, 1994 Effective: May 28, 1994
RA No. 8424	Gross selling price or gross value in money of shares of stocks sold, bartered, exchanged or otherwise disposed in accordance with the proportion of stocks sold, bartered or exchanged or after listing in the stock exchange. • Up to 25% • Over 25% but not over 33⅓% • Over 33⅓%	 4% 2% 1%	Approved: December 11, 1997 Effective: January 1, 1998

[6] Secondary offering refers to offering of stock to the public made after the IPO. (BIR Revenue Regulation No. 3-95)

[7] Revenue Memorandum Circular No. 21-08, March 12, 2008.

The lowering of the tax base under Section 127 (B) of RA No. 8424 is meant to attract more closely held corporations to go public and encourage investors to participate in public offerings. The change is also intended to enable small and medium enterprises (SMEs)[8] and those from the low-income sectors to participate actively in the development of the capital market.

C. IPO Transaction Costs[9]

Aside from the IPO tax, IPO transactions are also subject to various fees and charges imposed by the Securities and Exchange Commission (SEC) and the PSE.

1. Listing Fees for IPOs

SCHEDULE OF LISTING FEES

Type	First Board and Second Board	SME Board
Processing Fee	₱50,000 plus other incidental expenses.	₱20,000 plus other incidental expenses.
Initial Listing Fee	First ₱15 billion: 1/10 of 1% or ₱500,000 whichever is higher. In excess of ₱15 billion: ₱15 million plus 1/20 of 1% of excess over ₱15 million.	₱50,000 If the company fails to pay within the prescribed period, a surcharge of 25% plus 1% interest (based on the listing fee) for everyday of delay shall be imposed. (Note: This is also applicable to the First and Second Boards for IPOs and Listings by way of introduction.)

Note: Processing fees are non-refundable. All fees (listing and processing) are subject to the applicable value added tax (VAT).

[8] Small and medium enterprise is defined as any business activity or enterprise engaged in industry, agribusiness and/or services whether single proprietorship, cooperative, partnership, or corporation whose total assets, inclusive of those arising from loans, but exclusive of the land on which the particular business entity's office, plant and equipment are situated must have value falling under the following categories: Micro: ₱3,000,000 or less, Small: ₱3,000,001- ₱15,000,000 and Medium: ₱15,000,001- ₱100,000,000. (Magna Carta for SMEs).

[9] PSE Fact Book 2008.

2. Annual Listing Maintenance Fee

An annual listing maintenance fee (ALMF) is charged each listed company where the rate depends on the company's market capitalization. The ALMF is exclusive of the VAT.

First Board and Second Board	**SME Board**
1/100 of 1% of market capitalization but in no case to be less than ₱250,000 nor more than ₱2 million for each listed company.	₱100 for every ₱1 million market capitalization of listed shares as of the last trading day of the immediately preceding year, but in no case shall it be less than ₱50,000 nor more than ₱250,000.

3. SEC Fee

The Exchange collects from each of the buying and selling stockbroker a fee of 1/200 of 1% of gross value (excluding taxes and other fees) to be transmitted to the SEC.

4. Philippine Depository and Trust Corporation (PDTC) Fee

The PDTC charges a depository maintenance fee of 0.01% per annum or 0.0008333% per month based on the market value of holdings as of month-end effective May 1, 2005.

5. Brokerage Commission

A stockbroker is compensated for his/her services in executing orders on the Exchange through commission charges, which are paid by both the buyer and seller to their respective brokers. The minimum commission rates depend on the amount of the transaction.

Transaction Value	Minimum Commission[10]
₱100 million and below	0.0025 + 12% VAT
Above ₱100 million up to ₱500 million	0.0015 but not less than ₱250,000 + 12% VAT
Above ₱500 million up to ₱1 billion	0.00125 but not less than ₱750,000 + 12% VAT
Above ₱1 billion up to ₱5 billion	0.001 but not less than ₱1.25 million + 12% VAT
Above ₱5 billion up to ₱10 billion	0.00075 but not less than ₱5 million + 12% VAT
Above ₱10 billion	0.0005 but not less than ₱7.5 million + 12% VAT

6. Other Expenses

All other incidental expenses borne by the Exchange in the conduct of its due diligence in processing the application of the applying company shall be charged to the latter.

III. COMMENTS AND OBSERVATIONS

A. IPO versus Private Placement

Companies choose to go public for a number of reasons. They want to raise funds or to secure more financing when their sources have dried up. Going public is oftentimes the most practical and easiest way to raise new capital that can finance expansion or support a new venture.

Another reason is to allow the company's shares to become a much more valuable "currency".[11] As a public company issuing shares to raise more capital or granting stock options to entice employees to stay in the company, the company's

[10] The minimum commission rates were made effective on October 2, 2008 and subject to further action by the Securities and Exchange Commission per Memorandum for Brokers No. 2008-0467. The said rates shall not apply to broker-to-broker or odd lot transactions. In all cases, the provision of Presidential Decree No. 154 shall prevail over the commission rates set by the Board.

[11] Initial Public Offerings, FAQs, http://www.catalyst-law.com/document/25.

shares become much more valuable to the recipient because the latter know that they can easily sell or convert the shares into cash in the future when the need to do so arises.

The benefits of going public, however, have to be weighed against the costs associated with doing so. While it is true that in an IPO, funds are raised from the general public, the cost of raising funds is still comparatively high. The cost of an IPO normally depends on the size of the issue and the level of the marketing effort. Among the major expenses of an IPO are: (1) Issue manager, underwriting and selling and/or issue management fees; (2) Legal counsel and/or legal adviser’s fees; (3) Reporting accountant’s fee and receiving or agency fee; (4) Asset appraiser’s fee and auditor’s fee; (5) Promotion and publication’s expenses; (6) Administration and sundry expenses; and (7) PDTC Fee.

On the other hand, in a private placement, funds are raised from a small group of investors without resorting to underwriting. The cost of the issue in this case is very minimal. The sale of shares of stock is disposed of over the counter which is subject to the capital gains tax at the rate of 5% for shares of stock amounting to not more than ₱100,000 and 10% on any amount in excess of ₱100,000.

However, there are several advantages of trading through the stock exchange than over the counter. For one, if a company is listed in the Exchange, investors will pay more for its shares than they would if the shares are private because it is much more difficult to sell private company’s shares.

Moreover, it may be noted that stocks liquidated outside the PSE are deemed counterproductive as companies would only be attracting limited and small stakeholders. Trading at the Exchange would make trading efficient, transparent and raise further additional or new capital. Although trading outside the PSE can raise new equity capital, the price of this additional capital has to be arrived at in an indirect and inefficient manner. This means that an estimate of the market value of new equity should be done in order to determine the value unlike when it is listed, market forces of supply and demand will determine the value of the new shares for the particular company.

Potential mergers and acquisitions are also made easy if the firm is publicly listed. The status and publicity of a company are enhanced and this makes it easier for other companies to notice and evaluate potential synergies. Public firms also project a higher profile than private firms. This is important in industries where success requires customers and suppliers to make long-term commitments. In fact, according to a PSE Official, going public tends to improve corporate behavior, increases employee commitment and expands business relationships.

Another cost associated with being a publicly-traded firm is the information disclosure requirements. A privately-closed corporation experiencing financial difficulties may succeed in hiding its true condition unlike a publicly-traded firm which cannot hide its predicaments from competitors and the public at large.

Also, owners of publicly-held corporations are under the scrutiny of stockholders and if the latter think that the former are not helping the company, they may put pressure for the owners' removal. In other words, if the company becomes publicly-held, control of the company is no longer in the hands of a few but is always at stake. The element of control is the main reason why closely held corporations or family owned-corporations do not want to go public. These corporations subscribe to the idea that selling shares to the public runs the risk of seeing their holdings diluted and under the scrutiny of their stockholders.

Overall, the net trade off to going public will generally be positive for firms with large growth opportunities and funding needs. On the other hand, it will be smaller for firms that have smaller growth opportunities, substantial internal cash flows, and owners who value complete control over the firm.[12]

B. IPO Trend (1990-2009)

The IPO tax is allegedly one of the reasons why companies are reluctant to go public. Hence, there is a need to examine if there is truth to this issue. The IPO trend will be used as a yardstick to determine whether the imposition of said tax has led to the decrease in trading volumes. The IPO trend is divided into two parts, the pre-IPO tax (1990-1993), and during the IPO tax implementation (1994-2009), viz:

Table 2. NUMBER AND VALUE OF IPOs, CY 1990-2009

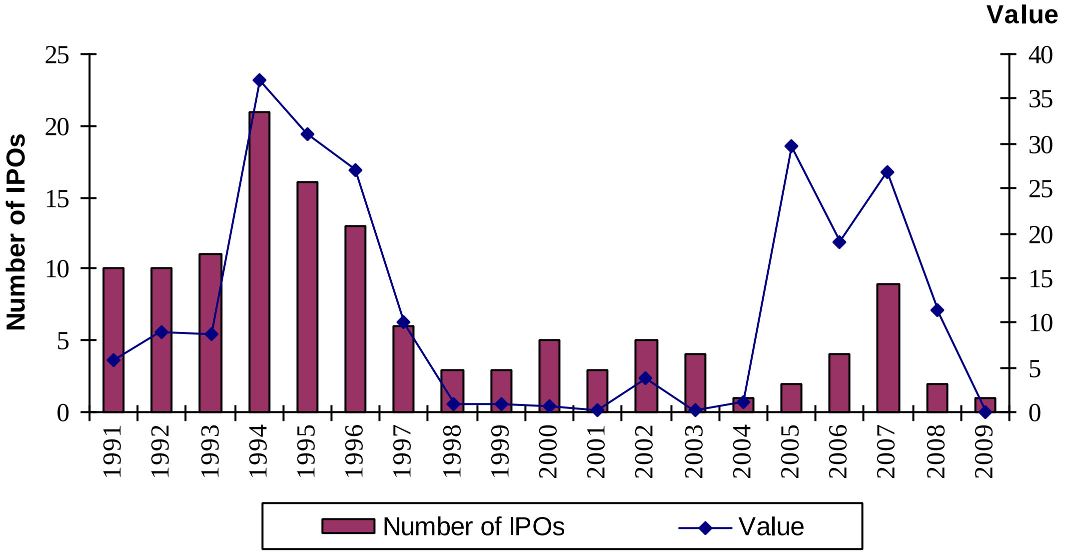
Year	Number of IPOs	Value (In Billion Pesos)
Prior to the IPO Tax		
1990	10	4.1
1991	10	5.7
1992	10	8.9
1993	11	8.7
TOTAL	**41**	**27.4**
With IPO Tax		
Under RA 7717		
1994	21	37.0
1995	16	31.0
1996	13	27.0
1997	6	10.0
TOTAL	**56**	**105.0**

[12] http://pages.stem.nyu.edu/unadamora/New_Home_Page/instables/ipo.htm.

Year	Number of IPOs	Value (In Billion Pesos)
Under RA 8424		
1998	3	1.0
1999	3	0.8
2000	5	0.6
2001	3	0.2
2002	5	3.9
2003	4	0.2
2004	1	1.1
2005	2	29.8
2006	4	19.0
2007	9	26.8
2008	2	11.4
2009	1	0.02
TOTAL	**42**	**94.82**

Source: PSE.

Figure 1. % Change in the Number and Value of IPOs



As noted in Table 2 and Figure 1, the year 1994 posted the highest number of IPOs (21) and correspondingly, the highest in terms of value (₱37 billion). It is also in the same year when the IPO tax was first implemented. However, the 91% increase (from 11 to 21) achieved in 1994 decreased by 24% and 19%, in 1995 and 1996, respectively. From the 1996's 13 companies, only six (6) companies undertook IPO in 1997, giving a decrease of 54%, and from 1997 onwards, the number of IPOs reached a single digit.

The number of IPOs almost remained stagnant in spite of the lowering of the IPO tax base effective January 1998 under RA No. 8424. With a total of 42 IPOs from 1998 to 2009, there was a decrease of 25% from the 56 IPOs covering the period 1994-1997. Thus, the objective of lowering the IPO tax base to attract more closely-held corporations to go public under RA No. 8424 was not achieved.

It seems that there is no direct relationship between the IPO tax and trading volumes. From the figures alone, as shown in Table 2, there has been a 37% increase in the number of IPOs (56) during the first four (4) years of the imposition of the IPO tax as compared to the four (4) years (41 IPOs) prior to its introduction. The values of IPO under RA No. 7717 (P105 billion) are likewise four (4) times the amount of IPO from 1990-1993 (P27.4 billion) which is prior to the IPO tax. However, IPO transactions under RA No. 8424 pale in comparison with IPO's accomplishment during its maiden years under RA No. 7717. IPO transactions from 1998-2009 only reached 42 IPOs amounting to P94.82 billion only. Therefore, in totality, the value of IPOs moved to the opposite ways as it increased when the IPO tax was first imposed and decreased at the time when the tax base was lowered.

At this point, it is perhaps relevant to determine the reasons behind the seemingly lackluster performance of the IPO especially during the implementation of RA No. 8424.

The dull performance of the IPO was first felt during the latter year of the effectivity of RA No. 7717 which is 1997 where there were only six (6) companies that went public. The Asian financial crisis started in July 1997 and affected not only the country's domestic capital market but those of the neighboring countries as well. From 1998-2006, not more than five companies went public. While nine (9) companies undertook IPO in 2007, the trend did not last as barely two (2) and one (1) companies in 2008 and 2009, respectively, went public.

There are events in the past which have made IPO even more unattractive. There was the impeachment saga in 2000 that brought about political instability in the country. The domestic capital market suffered as there was a massive withdrawal of investment and a continued downfall of the peso as against the dollar. The political uncertainties and poor economic environment went on up to 2004 which made some companies like telecommunication firm Smart Communications, Inc. rethink or defer their stock offerings.[13]

The local bourse saw light in 2005 when two (2) IPOs [Manila Water Company Inc. and SM Investments Corporation (SMIC)]were successfully undertaken. SMIC alone raised P28.75 billion in proceeds, the largest in the Philippines and considered one of the biggest in Asia at the time of the offering.[14] The Pilipinas Shell Petroleum Corp., on its part, did not respond to the pressure to go public because the market has been suffering from political and economic downtrends like the wiretapping scandal during

[13] "Smart to seek NTC nod on deferment of stock offering", http://money.inq7.net/topstories/view_php?yyyy =2004&mon=03&dd=06&file=4,, March 05, 2004.

[14] http://www.pse.com.ph/html/MarketInformation/pdf/factbook/PSE%20Fact%20Book%202005.pdf.

the 2004 election. The market's performance was dampened further by the temporary restraining order issued by the Supreme Court on the value-added tax, which would have brought an additional P5 billion worth of revenues a month to the government.[15]

In 2006, it may be said that the local bourse is still on a positive note when IPOs in this year generated P19 billion from the four firms that went public. Granting this is lower than the P29.8 billion IPO value in 2005, the figure is still robust compared to the value of previous IPOs.

Moreover, in 2007, nine (9) companies went into IPO. Their initial public offerings netted P26.8 billion. Insiders marked the year 2007 as the return of the IPO fever with the local stock market rising to a record high. The booming IPO market was attributed to the growing economy, low interest rate regime, and substantial remittances from Filipinos living or working abroad. The bullish sentiment of investors has enticed more companies to sell their shares to the public. The market's vigor and resilience gave these companies added confidence to tap the capital market for funds.[16]

However, in 2008, the PSE reported that the combined net income of listed companies went down by 29.4% despite a 12.8% increase in their aggregate revenues as rising costs padded their expenses. Two companies, namely Pepsi-Cola Products Philippines, Inc. (PIP) and San Miguel Brewery, Inc. (SMB), listed on the Exchange through IPO and the total capital raised from both IPOs amounted to P1.95 billion.[17]

Given the above, it can be said that the decision to go public is, more than anything else, influenced by several factors. The intention of the company to go public is dependent on external factors such as political uncertainties, economic environment like volatility of the exchange rate, interest rates, poor market condition, among others. Timing is also a crucial factor in order to achieve a successful IPO. Many studies proved that firms condition equity offerings on market return. Loughran, Ritter, and Rydqvist (1994) find that IPO volumes are higher following periods of high market return. Baker and Wurgler (2000) conclude that firms issue more equity after a year of high return and before years of low market return. In a much later year, Lowry (2002) notes that a higher market-wide market-to-book ratio and higher market return are associated with higher IPO volume. Therefore, firms condition their equity offering on market return because a high market return indicates increases in investment opportunities or an increase in investors' optimism.[18]

Also, the need for fresh capital is not enough reason for a company to go public. Companies have to take into consideration a lot of internal and external factors surrounding them. One has to scrutinize and check if the company, as well as its key

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[15] Cai U. Ordinario, "Shell to list after review of refinery", http://www.manilatimes.net/national/2005/jul/07/yehey/business/2005070bus10.html, July 7, 2005.

[16] Zinnia B. Dela Peña, "2007 Marked Return of IPO Fever to Stock Market", December 29, 2007.

[17] Philippine Stock Market Perfomance in 2008. (PSE 2008 Fact Book)

[18] Mingsheng Li, "A Better Understanding of Initial Public Offering Process: Evidence from Google", April 2005.

management personnel, is ready to go public. Strategic entry into the market is vital to the success of even the strongest IPO. A company that might easily attract public funds in a bull market could run into considerable resistance in a bear market. When the market becomes depressed, declines in value are generally greater for newer, less established issues and companies in "riskier" industries.[19]

The rigid listing and reportorial requirements imposed by both the SEC and the PSE on publicly listed companies may also be considered as one of the impediments in going public. Not to mention that the preparations for an IPO can be very time-consuming. It involves significant "housekeeping" of the company and priming of shares for sale, which can take anywhere from eight to 12 weeks, depending on the extent of corporate clean-up required. Thus, aside from the IPO transaction cost, too much documentation is needed prior to and even after an IPO, effectively making an IPO an expensive and rigorous undertaking. Initially, the applicant must ensure that it complies with existing tax laws, rules and regulations and financial accounting standards. To go public, applicant-company must register and lodge its IPO securities with the Philippine Depository and Trust Corporation and strict compliance with the SEC's full disclosure rules, the Corporation Code and the Securities Regulation Code must also be observed.

C. Assessment of the IPO Tax

The IPO tax is one of the two taxes imposed on stock transactions. The IPO tax is one of the variant of a broader category of a Stock Transaction Tax (STT). An STT of various kinds has been a common policy tool throughout the world. In fact, more than 30 countries have made used of STTs to generate more revenues.[20] However, research made by the PSE has confirmed that there is no equivalent tax on IPOs that become listed in the Singapore Stock Exchange, the Hong Kong Stock Exchange, the Stock Exchange of Thailand, the Bursa Malaysia, or the Australian Stock Exchange.[21] At this juncture, an examination of the IPO tax collection from 1994-2009 is made in the light of the effort of the government to raise revenues to meet its expenditure programs. (Table 3)

[19] www.exenfm.com/training/pdfiles/course13.pdf.

[20] Robert Pollin and James Heintz, "Evaluation of a Proposal to Reinstate the New York Transfer Tax", April 2003.

[21] The Capital Market Development Plan: Blueprint for Growth and Expanded Contributions to the Philippine Economy, 2005-2010, page 25, June 30, 2005.

Table 3. IPO TAX COLLECTIONS VIS-À-VIS NG TAX REVENUE COLLECTIONS CY 1994-2009 (In Million Pesos)

Year	IPO Tax Collections	% Increase (Decrease)	NG Revenue Collections	% Share of IPO Tax To NG Tax Revenue
Under RA No. 7717				
1994	1,237	--	271,305	0.46
1995	947	(23.4)	311,784	0.30
1996	639	(32.5)	367,894	0.17
1997	337	(47.3)	412,931	0.08
TOTAL	3,160		1,363,914	
Under RA No. 8424				
1998	169	(49.9)	416,587	0.04
1999	1,791	959.8	431,921	0.41
2000	632	(64.7)	460,034	0.14
2001	526	(16.8)	485,220	0.11
2002	364	(30.8)	496,371	0.07
2003	421	15.7	538,020	0.08
2004	609	44.7	598,014	0.10
2005	261	(57.1)	705,615	0.04
2006	88	(66.3)	859,857	0.01
2007	679	671.6	932,928	0.07
2008	279	(58.9)	1,049,189	0.03
2009	397	42.3	982,202	0.04
TOTAL	6,216		7,955,958	

Source of basic data: BIR.

It was in 1994, when the IPO tax was first introduced, and in 1999 that the government's collection of IPO tax reached billions of pesos as compared to other years' million peso collections. The lowest IPO tax collected was recorded in 2006 with only ₱88 million. IPO tax collection from 1998-2009 totaled ₱6.216 billion or an average of ₱518 million as against the ₱3.160 billion collection or an average of ₱790 million from 1994-1997.

Ever since its conception, the IPO tax shared an average of 0.12% of national government's revenue collection with the highest share of 0.5% in 1994 and the lowest share of 0.01% in 2006. Albeit, the IPO tax collection seems to be miniscule as compared with other national taxes, it still helps in the revenue generating effort of the government especially in the years when the country is facing huge fiscal deficits. Being a transaction tax, however, it cannot be relied to become a major revenue source.[22] This is because the tax is dependent only on the incidence of IPO transactions and the value thereof.

It may be worth mentioning that there have been some inconsistencies with regard to the collection of the said tax. There have been years when IPO tax collection fell down despite the increase in the number of companies undertaking IPO as well as the value of the IPO transaction. In 2002, the number of companies went up by 67% [from three (3) in 2001 to five (5)] with value increasing by almost 20 times from the previous year's IPO value (₱0.2 billion in 2001 to ₱3.9 billion in 2002) but still tax collection decreased by 31%. In 2005, there were two companies that went public from one in 2004 with value increasing to ₱29.8 billion as against the ₱1.1 billion IPO value in 2004 but tax collection dipped by 57%. The opposite was seen in 1999 and 2003 where collections went up even if the IPO value went down. In 1999, the IPO tax collection reached a record high of ₱1.8 billion with the number of companies going public remained the same as in the previous year but the value decreased to ₱0.8 million as against 1998 value of ₱1 billion with IPO tax at ₱169 million. The same scenario was seen in 2003 where both the number of companies and IPO value decreased while tax collection moved in reverse proportion. However, in 2007, tax collection escalated by 672% but the IPO value during said year was 59% lower than that of the 2005 value (₱29.8 billion in 2005 as against ₱26.8 billion in 2007) but collection in 2005 was only ₱261 million as compared to the ₱679 million in 2007. The collection from IPO tax further decreased in 2008 by 58.9% following an IPO of only two companies. However, revenues from IPO tax slightly increased by 42.3% in 2009 (from ₱279 million in 2008 to ₱397 million in 2009) despite the fact that only one company ventured into IPO and its IPO value only amounted to around ₱20 million. It is worthy to mention that the payment of the IPO tax takes place within 30 days from the date of sale for primary offering and five (5) banking days from the date of collection for secondary offering.

The discrepancy in the tax collection of the BIR vis-à-vis the data on the number of companies and value of IPOs gathered from the PSE may have been due to the difference in the data recorded by the BIR and the PSE on the number of companies that went public from 1999-2004. The BIR's data listed more companies that went public compared to PSE's data. The BIR provided a breakdown of companies which went public on a monthly basis while the data supplied by the PSE consist of the name of the issuing company, name of stock, and value of total IPO (both primary and secondary listings). However, upon scrutiny of the records, it was found out that the names of companies provided by the PSE that went public from 1999-2004 were not even included in the BIR's list of IPO taxpayers.

It is thus assumed that the BIR's data only consist of secondary offerings where the IPO tax is being paid by the seller. The PSE only keeps track of the names of participating companies. Per interview with an RDO Official in Pasig it was found out that there is no coordination between the BIR and the PSE with regard to the payment of any tax emanating from stock transactions because they have different mandates. The former's function is to collect taxes, and the latter has nothing to do therewith. In

[22] Maxim Shvedov, *"Transaction Tax: General Overview",* December 2, 2004.

view thereof, there is a need to reconcile data/information coming from the BIR and PSE in order to ensure that no one escapes the payment of the IPO tax.

Moreover, one of the reasons for the low IPO tax collection is because of rampant incidence of backdoor listings in the market. Backdoor listing is a practice wherein capitalists take a dormant or illiquid company, allowing them to list their shares and raise capital in the stock market without going through the tedious listing process and the payment of the IPO tax and other fees and charges associated with an IPO.

Based on the foregoing, the IPO tax is not the only factor that influences IPO transactions. As reiterated, the IPO trend is dependent on several factors aside from taxation. In fact, data show that the increase or decrease of IPO tax collections is not altogether dependent on the number of IPO transactions but on the value thereof. Thus, there can be an instance where even a single IPO could raise substantial revenue.

D. Proposed Elimination of the IPO Tax

As mentioned earlier, the IPO tax is being pinpointed as one of the major factors restraining market efficiency. Back in 1997, the PSE favored the scrapping of the IPO tax which is then paid by the issuing corporation in the case of primary offerings or by the seller in the case of secondary offerings.[23] In the same year, the Department of Finance (DOF) reviewed the proposed abolition of the IPO tax but this did not prosper due to the increasing fiscal deficit of the country. The Asian Development Bank (ADB) also urged the government to abolish the 1%-4% tax levied on all initial public offerings to boost liquidity in the equities market. Likewise, a study conducted by the Capital Market Development Council (CMDC) proposed to scrap the taxes imposed on companies that go public to further spur the growth of the local equities market. It noted that the removal of the tax on IPOs will encourage more investors to park their funds at the local bourse. As argued by the CMDC, the IPO tax acts more as a deterrent to IPO because it is a tax on capital and not on income.[24] Even in other countries there have been measures to either reduce or eliminate their STTs due to the perception that taxes were contrary to the priority of allowing financial markets to operate in an untrammeled fashion.[25]

While the government's aim in imposing IPO tax is to raise revenues, it is also not in any way, meant to discourage investors' active participation in the capital market. It may be recalled that prior to the imposition of the IPO tax, shares of stock in companies were treated like any other personal or movable piece of property. That is, no gain or loss is recognized when the stocks acquire or lose value as a result of the operations of the unlisted corporation as long as the shareholder holds on to the stock. Gains or losses on stocks are only "realized" when these are sold or exchanged. The

[23] Fil C. Sionil, "DOF Orders Review: Abolition of IPO tax is under study", Manila Bulletin, February 13, 1997.

[24] Iris C. Gonzales, "Scrapping of IPO taxes urged", Philippine Star, page B1, July 10, 2007.

[25] *Pollin and Heintz, op. cit. p.3.*

gain of the investor is to be reported as part of the taxpayer's gains from the sale or exchange of capital assets during the year and part of gross income subject to the regular income tax. It was in December 1970 via the passage of RA No. 6141 that shares of stock listed in the stock market were taken away from the coverage of other transactions within the scope of the regular income tax and given a different tax treatment. This move was made in order to develop the capital market. Since then the percentage of the tax on stock market transactions moved several times, but within the range of a low 0.25% to a high 2%.

Not for long, transactions in shares of stock that were not listed in the Exchanges were likewise removed from the scope of income subject to the regular income tax and were also given a separate tax treatment. Before the Comprehensive Tax Reform of the Philippines (CTRP), capital gains tax (CGT) on sale of shares not traded in the stock exchange stood at 10% on the first ₱100,000 of net gains on sale or exchange of shares of stock of unlisted companies and 20% on the excess.

The difference between the tax on gains on the sale of unlisted shares as against that of listed shares led to opportunities for abuses as owners of companies saw the opportunity by offering only a minimal portion of their shares of stocks to the public just to be said that the company has "gone public". Not only did they remain in control of their corporation but more so they were only subjected to the STT rather than the CGT which was then leveled at a maximum of 20% on the gross amount of gains. This became an avenue for owners of companies to offer their shares of stock to the public and be subject to a much lower STT. The IPO tax, thus, levels the playing field and ensures that substantial amount of equity is offered to the public to be truly characterized as a publicly-held company.

The IPO contributes a great deal in the development of the economy. Its importance in growing the capital market cannot be denied. This is probably one of the reasons why there are companies mandated by law to offer a certain percentage of their shares to the public. Among these are: (1) the Board of Investments (BOI)-registered enterprises where under EO No. 226 (Omnibus Code of the Philippines), a registered enterprise, unless otherwise exempt, shall at any time within ten (10) years from the date of its registration, be required by the Board to offer for sale to the public[26] ten (10%) percent or more of its total subscribed capital stock, voting and non-voting, and any increase thereof; (2) the oil-refinery businesses under RA No. 8479[27] which states that any person or entity engaged in the oil refinery business shall make a public offering through the stock exchange of at least 10% of its common stock within a period of three (3) years from the effectivity of the Act; and (3) the telecommunications companies under RA No. 7925[28] which provides that in compliance with the Constitutional

[26] The term "public" shall include alien investors; however, the first three (3) months of the public offering shall be limited to Filipinos: Provided, That the period of public offering shall be at least six (6) months from date of publication. (Rule VIII, Implementing Rules of E.O. 226).

[27] "An Act Deregulating the Downstream Oil Industry, and for Other Purposes" approved on February 10, 1998.

[28] "An Act to Promote and Govern the Development of Philippine Telecommunications And the Delivery of Public Telecommunications Services", approved on March 1, 1995.

mandate to democratize ownership of public utilities, all telecommunications entities with regulated types of services shall make a bona fide public offering through the stock exchanges of at least thirty percent (30%) of its aggregate common stocks within a period of five (5) years from effectivity of the Act or the entity's first start of commercial operations, whichever date is later. The public offering shall comply with the rules and regulations of the SEC.[29]

The rationale behind the mandatory IPO of the companies mentioned above is to democratize and broaden their base of ownership. It is observed, however, that most publicly listed companies issue only up to 10% of their total shares to the public. As a result, most listed companies remain to be controlled by their largest shareholders or a few wealthy groups/individuals.

The country is in dire need of revenues to pursue its developmental programs and to continuously deliver basic social services. The country is facing serious budget deficit at the moment and the removal of any tax may only create further economic doldrums. It would also be difficult for the government to replace the revenue to be waived from the IPO tax. Presently, the IPO tax is the only tax imposed on IPO transactions after the documentary stamp tax (DST) on stock transactions has been permanently abolished per RA No. 9648.[30]

Further, the increase in the cost of financial transaction brought about by the IPO tax would not dissuade genuine companies from going public as said tax is only a portion of the transaction cost borne by companies and cannot bring the stock exchange to a standstill. Except perhaps for SEC fees, all transactions costs tied with IPO transactions are fees and charges that do not go to the national coffer. Hence, the claim that the IPO tax serves as a deterrent for companies to engage in IPO seems to be a sweeping statement and does not stand on a solid ground.

E. Practices in Other Countries

In other countries like Japan, Singapore, Portugal, Sweden, Ecuador, Denmark and Germany, no securities transaction tax (STT) is levied on stock transactions. There is no IPO tax either in said countries. In neighboring countries like Korea, Malaysia, Japan, China, Hong Kong, and Singapore, the common transaction costs associated with IPO activity are brokerage commission, initial listing fees and annual listing fees

The practice of tax-free stock transaction in some countries attracts investors, both foreign and local. On the other hand, among the countries in the Asia Pacific Region that levy the STT, the Philippines, China, Malaysia and India have the highest

[29] Ibid. Sec. 21.

[30] "An Act Exempting From Documentary Stamp Tax Any Sale, Barter or Exchange of Shares of Stocks Listed and Traded Through the Stock Exchange, Further Amending for the Purpose Section 199 of the National Internal Revenue Code of 1997, As Amended by Republic Act No. 9243, and For Other Purpose. (June 30, 2009)

rate of 0.5%, followed by Korea, Taiwan, Australia, Hong Kong and South Korea which collect a 0.3%.

The PSE is lagging behind the country's neighboring stock exchanges in terms of wide range of products and services being offered in their bourses that help contribute to the vibrancy and sophistication of their financial services. Table 4 depicts the number of companies that went public in selected ASEAN countries:

Table 4. NUMBER OF IPOs IN SELECTED ASIAN COUNTRIES

Number Of IPOs	Malaysia	Thailand	Hongkong	China (Shanghai)
1997	88	5	82	-
1998	28	1	32	-
1999	21	-	31	-
2000	38	2	43	-
2001	20	7	31	-
2002	51	18	60	86
2003	58	21	46	93
2004	72	36	49	83
2005	79	36	57	87
2006	40	12	56	94
2007	26	7	81	65
2008	23	9	49	88
2009	14	7	73	-
TOTAL	**558**	**161**	**690**	**596**

Source: Various stock exchanges.

IV. CONCLUSION AND RECOMMENDATION

IPOs are considered as the lifeblood of any expanding and developing stock market. However, these have not yet contributed much to the growth and development of the country's local stock exchange. PSE insiders believed that the tax imposed on the sale of shares of stock through IPO discourages many companies to go public. Consequently, the growth and development of the capital market is adversely affected. However, the unimpressive performance of the capital market or stock exchange at present cannot be solely attributed to the IPO tax. There are other factors like peso depreciation, continuing political and economic problems which serve to discourage investors to invest in the Philippine domestic market.

Based on the study, there is no direct relationship between the decision of companies to go public and the imposition of the IPO tax. In fact, the enactment of RA No. 8424 that led to the lowering of the IPO tax base did not, in any way, entice companies to go public. The persistent clamor to abolish the IPO tax at this point, therefore, seems impractical. The amount collected from the IPO tax is necessary as the country is finding it difficult to raise sufficient revenues to fund its expenditure programs through taxation. Further, the abolition of the IPO tax is not in conjunction with the need of the hour, which is to tax all sectors of the economy that remained undertaxed or not in the ambit of taxation. If the said tax will be removed, it would be difficult to reinstate it once the government deems it necessary to tax IPO transactions and would face more political pressures than the clamor for its abolition. .

Nonetheless, in order to fully maximize the collection of the IPO tax, the following suggestions may be made:

a. The PSE should not only keep track of issuing companies in primary offerings but also of sellers in secondary offerings and coordinate with the BIR in this regard in order for the latter to enhance its monitoring of the IPO tax;

b. The PSE, in coordination with implementing agencies like the National Telecommunications Commissions (NTC), BOI and the Department of Energy (DOE) should enjoin profitable companies registered with them to go public, particularly companies mandated by specific laws to offer a percentage of their stocks to the public, not only to increase collection of the IPO tax but also to improve the supply side of the market with a more diverse menu of stocks available to the public. For instance, there are at least 1,000 companies registered with the BOI, and if at least 10% of them list on the Exchange, it will increase the depth of the country's equities market; and

c. It is also further recommended that a review of the IPO requirements be made to make the same simpler and less tedious for participating IPO companies including the simplification of the disclosure process. The simplification of the listing criteria for the IPO should also be carefully studied to make the listing process more investor-friendly without sacrificing public interest/welfare and to further encourage public participation. There is also a need to re-examine other factors that affect the interest of potential IPO traders by closely monitoring trading practices in the Exchange and in foreign counterpart Exchanges to boost the growth and development of the Philippine stock market and make it globally competitive.

In sum, in the light of the allegation that the IPO tax affects the attractiveness of the country's equities, it is to be noted that any stock exchange in the world is susceptible to a number of internal and external factors that affect its performance as well as the confidence of investors. The prevailing price of the shares of stock in the market, the economic and political conditions of the country, the availability of cash reserves and the readiness of a company to go public, among others, are equally important considerations in venturing into IPOs. There is not one ingredient that can solve all of the problems besetting the PSE. However, elimination of the IPO tax at the moment is seen to be impractical and irrational as this would not only affect the revenue effort of the government but may also bring back the old practice of company owners engaging in IPOs even if they will only offer a minimal portion of their shares of stock to the public just to escape the payment of the CGT, which is a much higher tax than the IPO tax. If the IPO tax is used in conjunction with other policy mechanisms (e.g., banning of short selling and insider trading, etc.), the concerns of insiders would, thus, be minimized. This in turn would lead to the growth and development of the country's stock market.