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By ANDREW JAMES GERARD DULAY RUIZ

The value-added tax and Overseas Economic Cooperation Fund projects

In 2016, the Bureau of Internal Revenue (BIR) issued Revenue Memorandum Circular (RMC) 69-2016 (suspending the effectivity of all revenue issuances covering the period from 01 to 30 June 2016). Why? Per various newspaper articles, the BIR mentioned that they received reports alleging that some issuances were subject to "abuse", or unnecessarily difficult to comply with. Following this RMC, the BIR undertook a review of these (and other) particular issuances, to check if the issuances correctly interpreted the National Internal Revenue Code of 1997, as amended (Tax Code) and other tax related laws, if the issuances were possibly subject to abuse, and whether or not the issuances made compliance more difficult for taxpayers. We know that several issuances have been repealed, and some have been retained since then. Let's examine one particular issuance that, as a result of the continuing review, has been "amended, repealed or modified accordingly".

RMC 08-2017 clarifies the treatment of the value-added tax (VAT) on Philippine government money payments for Overseas Economic Cooperation Fund (OECF) projects under the Exchange of Notes between the Republic of the Philippines and Japan. Previously, RMC 45-2015 (which has the same stated subject matter/title) provided the method of treating the VAT regarding these projects. In these circulars, the term Philippines refers to the Philippine government or any of its political subdivisions, instrumentalities or agencies including government-owned

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or controlled corporations (GOCCs).

Both circulars recognized the Exchange of Notes between the two countries governing OECF projects, to the effect that the Philippines would assume all fiscal levies and taxes imposed in the Philippines on Japanese companies operating as suppliers, contractors, and/or consultants (contractors), "with respect to the payment carried out for and the income accruing from the supply of the products and/or services required for the implementation of the projects enumerated in the list". And that's basically where the similarity ends.

RMC 45-2015 cited the general rule of a final withholding VAT (FWV) of five percent provided under Section 114(C) of the Tax Code (previously creditable withholding VAT prior to Republic Act or RA 9337). Hence, RMC 45-2015 required the Philippines to withhold the five percent FWV on its gross payments for the projects, with this VAT to be paid out from the fund of the Philippines as a final settlement of the tax due on the income received by Japanese contractors. The Japanese contractors were then prohibited from including in its billing to the Philippines the whole twelve percent VAT that will be assumed by the Philippines.

Section 4.114-2 of the Consolidated VAT Regulations (RR 16-2005, as amended) further clarified that the five percent VAT represents the net VAT payable of the seller, and the remaining seven percent accounts for the standard input VAT for sales of goods or services to the Philippines, in lieu of the actual input VAT directly attributable or ratably apportioned to such sales. The result would be that if the actual input VAT attributable to sale to the Philippines exceeds seven percent of gross payments, the excess may form part of the Japanese contractor's expense or cost. If the actual input VAT is less than seven percent, the difference must be closed to expense or cost, i.e., treated as income. Note that under the Exchange of Notes, the Philippines should also assume the income taxes. Clearly, the general rule of withholding the VAT under Section 114(C) of the Tax Code made for more complex compliance.

On the other hand, RMC 08-2017 basically returns to the old rules stated in RMC No. 42-1999 (02 June 1999):

1. The VAT-registered suppliers and sub-contractors of the Japanese contractors are allowed to bill and pass on the twelve percent VAT to the Japanese contractors, whereby the Japanese contractors shall include and pass on in their billings to the Philippines the 12 percent VAT. The VAT will be for the account of the Philippines.

2. The Japanese contractors shall file the prescribed VAT returns on the gross receipts derived from the projects, claim the input taxes from their purchases of goods, properties and services from their suppliers or subcontractors and shall pay the output tax or VAT thereon, after offsetting the creditable or allowable input taxes. In any case, the amount intended for payment of the VAT would have been already been collected and received by the Japanese contractors as part of the total billing/invoice price (passed on to the Philippines).

RMC 08-2017 provides an additional qualification, i.e., that in no case shall input taxes arising from transactions attributable to activities unrelated to the project be allowed or be credited against the output tax on gross receipts from the project. However, it should be noted that RMC 08-2017 further differs from RMC 42-1999, as follows:

- RMC 42-1999 expressly stated that the Japanese contractors are exempt from the requirement of withholding VAT under Section 114(C) of the Tax Code. Note that this RMC did not state that the Japanese contractors were exempt from the VAT; and
- RMC 42-1999 provided for the means of recovery of the VAT which may have been previously withheld.

With no mention of the general rule of FWV provided in Section 114(C) of the Tax Code, it appears that RMC 08-2017 has simplified compliance requirements for these transactions. However, wouldn't it have been clearer if the RMC did restate the exemption of these transactions from the FWV? Can the BIR consider going further, examining in-depth the bases (then and now) for the statements in RMC 42-1999? For example:

a. Can an argument be made with regard exemption from the FWV, using the Exchange of Notes as "part of the law of the land" (Bayan Muna vs. Alberto Romulo and Blas F. Ople, G.R. 15968, dated 01 February 2011). Since the Philippines will assume all the fiscal levies and taxes, there is no need for the system of withholding tax,

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creditable or final, to collect from the Japanese contractors. After all, Section 114(C) of the Tax Code merely provides a method of collection or a more simplified VAT withholding system, whereby the Philippines is constituted as a withholding agent with respect to its payments for goods and services (ABAKADA Guro Party List vs. Eduardo Ermita, G.R. 1608056, dated 01 September 2005).

b. Knowing the previous level of tax compliance imposed on taxpayers, it is logical to presume that the Philippines complied with the five percent FWV. If after computing the total VAT liability of Japanese contractors (including the five percent FWV which may have been previously withheld), the result is still that the Japanese contractors incurred excess VAT payments, shouldn't the excess be allowed as a refundable VAT (subject to existing laws, rules and regulations)?

We welcome the review process being undertaken by the BIR, as well as the prospects for the reform of our cur-

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rent tax system. Being conscious of the results of these reviews, as well as the progress of the proposed reforms, amplifies our appreciation of these efforts, as well as our understanding of the need to be involved in the processes so as to arrive at informed and genuine reforms.

Andrew James Gerard Dulay Ruiz is a director from the Tax Group of KPMG R.G. Manabat & Co. (KPMG RGM&Co.), the Philippine member firm of KPMG International. KPMG RGM&Co. has been recognized as a Tier 1 tax practice, Tier 1 transfer pricing practice, Tier 1 leading tax transactional firm and the 2016 National Transfer Pricing Firm of the Year in the Philippines by the International Tax Review.

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