AMCHAM PHILIPPINES
The American Chamber of Commerce of the Philippines, Inc.

August 5, 2014

Hon. Enrique Cojuangco
Chairperson, Committee on Economic Affairs

Hon. Mark Villar
Chairperson, Committee on Trade and Industry
House of Representatives
Quezon City, Philippines

Dear Chairpersons Cojuangco and Villar:

Thank you for inviting us to this public hearing on House Resolutions 666 and 746, inquiring into the state of preparedness of the Philippines for the new obligations of the ASEAN Economic Community.

We are attending today not to discuss the potential effects, positive or negative, of the AEC economic integration to individual sectors, but to inform Congress of the view of foreign business chambers that AEC, AFTA, and related free trade agreements present enormous opportunities to Filipino companies, no matter how large or small, to grow larger through exports to billions of customers by taking advantage of these free trade agreements. Foreign investors operating in the Philippines are also able benefit from the AEC and these FTAs.

Unprecedented Opportunities to Export

The population of the AEC economies exceeds 625 million. Add Australia, China, India, Korea, Japan and New Zealand, and the total population of potential customers is over three billion. Free trade with these economies gives Philippine exporters unprecedented access to extremely large markets but also increases the exposure of domestic Philippine markets to imported products. On the one hand, the Philippines has new opportunities to provide large quantities of food and manufactured products, as well as services, to new consumers with rising incomes. On the other hand, the survival of domestic firms may be challenged by inexpensive imported products and regional service providers.

The Philippine Government has for several years been informing businesses - especially SMEs - of the new opportunities and challenges, while also developing – in consultation with the private sector - strategies to deal with potential threats to domestic production.

We commend the DTI for the roadmaps they are conducting for nearly 50 industries - including 7 for agribusiness - in which export potential is evaluated and needed reforms and incentives are identified. (List of roadmaps is attached at Annex A). These roadmaps, when implemented will prepare these sectors better to take advantage of the opportunities of new FTAs. We encourage committee members to inform themselves of details of these roadmaps as they are completed.

Public Sector Are Essential to Reducing Business Costs and Philippine Competitiveness

Mr. Chairmen, we urge your Committees to study and advocate practical solutions to improve the investment climate by **reducing or removing impediments placed by the public sector** that hinder firms in the Philippines from fully realizing the potential of these FTAs.

We would like to discuss several categories of impediments, which increase the cost of doing business and make it difficult for domestic enterprises to compete with imports and exports competitively to foreign markets:

Power costs

Domestic businesses are handicapped by the high cost of electricity in two ways. First, power prices are higher than in most competing countries. Second, the government taxes power with a 12% VAT. As shown in the attached chart (see Annex B) from a joint study by International Energy Consultants and MERALCO electricity costs almost USD 0.20/kwh in the Philippines but is as cheap as USD 0.085/kwh in Indonesia. We would ask the Congress to study whether the VAT on power and fuel for industrial and commercial services should be waived.

Transportation costs

Congestion on roads and at airports and seaports adds to business costs and reduces competitiveness.

Seaports. As an archipelago, the Philippines faces different domestic transportation challenges than mainland Asia, economies that are linked together by road and rail, internally and across borders. The Philippines is dependent on efficient domestic shipping. While the government provides fiscal incentives to support new domestic ships, it imposes taxes on shipping services and shipping fuel, thereby raising the cost of shipping for local businesses. Also, unwarranted PPA fees and MARINA rules requiring overmanning of ships increase shipping costs.

Roads. Recently, the United Nations predicted that the Philippines will have almost 90 million people living in cities by the year 2050. As the country continues strong economic growth many more Filipinos can afford cars. This year the Chamber of Automotive Manufacturers of the Philippines, Inc. estimates 240,000 new vehicles will be on Philippine roads (see Annex C). By 2020, this will increase to 450,000 vehicles. While the DPWH is spending over Php 100 billion a year on roads and bridges, and expressways such as the Calamba-Laguna and Laguna Lakeshore are likely to be built in a few years, more and more road projects will be needed to accommodate the increasing number of vehicles.

Rail. A recent JICA study recommends a $60B program over a decade that emphasizes rail construction to move commuters in the NCR and adjacent provinces from motor vehicles to more efficient train travel. These projects are critical to create efficient transport systems and relieve congestion. Unfortunately, the Philippines has a record of very slow implementation of major projects, e.g. NAIA Terminal 3 took over 20 years and the construction of light rail projects is very slow. Only 4 new stations have been opened in the last 12 years and no new ones will be opened until 2018.

Seaports. In addition, the port infrastructure of Batangas and Subic should be better utilized and a cap should be placed on container traffic in the port of Manila to reduce congestion. We commend House Transportation Committee Chair Cesar Sarmiento for holding a hearing on August 6 on optimization of ports nationwide.

Holidays

The 20 non-working holidays in 2014 is 33% higher than the average of 15 days observed by our main regional competitors (see Annex D). Congress recently deliberated on two additional non-working holidays (HB 4478 - National Farmers and Fisherfolk Day every May 15 and HB 4113 - the post-election non-working holiday) and several more holiday bills are pending in Congress. When Congress passes laws of this nature, legislators signal they are insufficiently concerned with added cost to employers that leads to the loss of jobs. We urge your committees to file and enact the Holiday Rationalization bill filed by the late Rep. Salvador Escudero in the 15th Congress to address the negative effect of excessive non-working holidays on businesses.

Smuggling

Smuggling in the Philippines does not occur offshore or over remote beaches but in the ports of Manila, Batangas, Subic, Cebu, and elsewhere. There is a long history of illegal conduct by importers and their Bureau of Customs (BOC) collaborators. Aside from being unfair to government tax revenue, smuggling is unfair to businesses that follow the rules and pay the VAT, unlike their competitors who cheat the system. Investors in the country expect the public sector to enforce regulations on cross-border trade. The recent reforms of the leadership at the BOC should be strongly supported. The CMTA legislation being deliberated in the House Ways and Means Committee should be passed to support the modernization of customs procedures in accordance with international standards.

Taxes

High income and other taxes are disincentives to business. So too are time-consuming filing procedures. In the Philippines, the corporate income tax (CIT) of 30% is one of the highest in the region seen in Annex E. Hong Kong is the lowest at 16.5% and Singapore at 17%. In the US, the CIT rate is almost 40%, leading some companies to merge with foreign companies with lower tax regimes (i.e. the UK which has reduced its CIT to 20%). The Senate Ways and Means Committee has initiated hearings on lowering corporate and individual income taxes. We encourage more discussion of reforms to raise consumption taxes and reduce income taxes in order to incentivize hard work by individuals and investment by firms.

Although the adoption of electronic filing in 2012 reduced labor tax payments by 11 steps in the Philippines, the 2014 World Bank study on Paying Taxes shows that the country can still vastly improve in reducing time to comply (193 hours) and total number of payments (36), relative to ASEAN neighbors like Hong Kong, Singapore, and Malaysia. (See Annex F). The same study shows that total taxes—including on labor, profit, and other taxes—paid in the Philippines can reach up to as high as 44.5%, higher than the average of 36.4% in the Asia Pacific region. Hence, the Philippines continues to be in the lower half of the rankings of the ASEAN-6 in terms of paying taxes (see Annex F).

Regulations

Over the years, the Philippine bureaucracy has increased regulations on business activities with too few effort to reduce and simplify procedures. In 2007, R.A. 9485 or the Anti-Red Tape Act was enacted and has generally been effective in shortening the time government agencies approve routine permits and licenses. A decade ago, the Asian Development Bank conducted a survey on the main issues facing business and bureaucratic regulations came out as one of the main issues. The study stated, "According to the World Business Environment Survey in 2000, about 80% of firms report that up to10% of management time is spent for this purpose, while 20% of firms spend more than 10% of management time."[1]

[1] Philippines: Moving Toward a Better Investment Climate, pp. 20-21, ADB.

Indeed, the 2013-14 World Economic Forum Global Competitiveness Report shows that compared with other ASEAN-6 countries, the Philippines imposes a heavier burden of government regulations and, its business rules on FDI are also more restrictive (see Annex G). This is supported by the 2013-14 World Bank's Ease of Doing Business report showing that despite improving the ranking due to reforms in the bankruptcy law, the Philippines requires 15 procedures taking 35 days to start a business—a tedious process that ranks the country low and highly uncompetitive at 170 of 183 countries in starting a business.

As cited in a recent article by National Competitiveness Council private sector co-chair Guillermo Luz, the new Australian government has established two Repeal Days a year in Parliament when laws are wiped off the books in bulk. Australia's goal is to reduce the cost of compliance for businesses by A$1 billion a year.[2] The first Repeal Day was March 26 this year, when over 10,000 laws and over 50,000 pages of regulation were eliminated in the single largest bulk repeal in its history. This cuts the cost of compliance by A$700 million. The cuts are made in three lines: (1) cut duplication between and across agencies; (2) streamline onerous and costly procedures; and (3) take a common-sense approach to regulations. The purpose is to cut unnecessary legislation and costly regulations and reduce the cost of doing business.

A similar program undertaken in the Philippines would be extremely helpful in reducing bureaucratic burdens on business that increase costs and reduce competitiveness. Conducting business-to-government activities online reduces business costs greatly and can be done at every level of government. It should be required that forms be downloaded and completed online and for payments to and from the government be made electronically. Such reforms will save time and transportation costs. In this regard we commend the reform by BOC Commissioner Sevilla to accept electronic filing exclusively by the end of 2014.

Business consultant Peter Wallace has recently written about excessive red tape for power plants in a paper, from which the following is excerpted:

> "But why does it take the government … more than 3 years to approve the construction of a power plant? In WBF's Quarterly Roundtable, the DOE pointed out that there are **165 signatures** needed to secure the necessary permits to build plants! Yes, you read it right: 165. This Red Tape entangled all over the country's future power infrastructure is jeopardizing the country's potential growth. There is enough interest to build plants in the country, but building a power plant takes at least 3-5 years and in the Philippines many times it is longer than that to even get started."

Internet speed

The miracle of the Internet enables rapid and inexpensive communication almost anywhere, almost anytime, and by almost anyone. Filipinos adapt to communications technology rapidly, the latest example being the use of smartphones as their cost rapidly falls. However, smartphones with their access to the Internet are most beneficial if broadband speeds are higher, and the Philippines is badly lagging in this respect. A HK survey showed that internet speed in the Philippines is the slowest among ASEAN member nations (see Annex H). One way to encourage better communication infrastructure is to reform the telecommunications investment environment to have more competition leading to better service and lower prices by amending the Public Services Act to remove telecommunications as a public utility. This would allow foreign firms to own more than 40% equity as is the case of most countries in the world. A World Bank survey of 84 countries shows only Ethiopia is more closed than the Philippines (See Annex I).

[2] Philippine Daily Inquirer, Repeal laws and lower cost of doing business, March 29, 2014.

Conclusion

The potential for the Philippines is enormous. With the country's population projected to grow to 140 million by 2050, the principal challenge to the Philippine Government in the future will be to provide better quality jobs to additional tens of millions of Filipinos entering the workforce in the next several decades. Many of these future jobs can be created in export industries within ASEAN and to other economies that are linked to ASEAN through FTAs. The country cannot stand still in an increasingly competitive, globalized trading environment but instead must continuously improve its competitiveness against other economies that are not standing still.

In this regard we share copies of the *Arangkada Philippines* 2013 Assessment.

This, in short, is the best answer to the subject of the resolution before the committees on "maximizing the benefits the AEC brings."

Sincerely,

Mr. John D. Forbes
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The *Arangkada* Philippines Project