AMERICAN

AUSTRALIAN - NEW ZEALAND

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JAPANESE

August 24, 2020

(May 27 letter updated with 6 additional signatories and italicized textual comments)

Sen. Pia Cayetano
Chairperson
Committee on Ways and Means
Senate of the Philippines
Pasay City, Manila

Dear Sen. Cayetano:

We write to supplement and replace our March 3 letter and to include new observations and recommendations on SB 1357, the committee report on the CITIRA. We submit these comments in the cooperative spirit of our meetings to discuss the legislation.

We understand the legislation will be renamed the Corporate Recovery and Tax Incentives for Enterprises Act (CREATE) and contains several new provisions, which will appear in the committee's substitute bill. Comments in this paper are based on the July 30 draft which was shared with us.

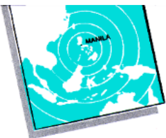
Our letter is divided into four parts:

1. the New Normal: the world and the Philippines face their gravest crisis since WWII,
2. Vietnam, India, *and Indonesia* are big winners from the shift away from China,
3. CITIRA/*CREATE*: content and timing, and
4. SB 1357: comments, proposed rewording, and amendments

1. New Normal: the world and the Philippines face their gravest crisis since WWII

On March 31 United Nations Secretary General Antonio Guterres warned that the world faces its most serious crisis since World War II as a result of a pandemic that will cause a recession "that has no parallel in the recent past."

The Asian Development Bank estimated that global GDP could fall as much as 9.7% or losses of $8.8 trillion over 6 months in a report released May 15. As many as 242 million jobs could be lost. With more than 5.5 million confirmed cases and



total deaths near 350,000,[1] the harm to the health of the world's population will contintue to mount until treatment remedies and vaccination protection are available.

The Philippine population is gravely impacted by the COVID-19 enemy. Lives and livelihoods of citizens and the life of the economy are continually beng harmed during the quarantine and recovery under the "New Abnormal."

No one knows when the old normal will return, with or without a second or even third wave of infection, or whether recovery will be a V, W, or U or fall into a "doom loop" and not recover for many years.

NEDA reports that 18 million households, 80% of all households in the country, require assistance. In early May the trade union group Nagkaisa estimated more than 2 million workers in the formal sector have lost their jobs. Similar numbers of informal and daily workers have little or no income. Hundreds of thousand of OFWs are coming home. Unemployment levels will reach double digits until the economy recovers. In Senate hearings on May 21 DOLE Secretary Bello agreed that job losses could reach as high as 10 million.

NEDA reported a quarterly GDP growth rate of -0.2% for First Quarter of 2020, ending an 84-quarter growth streak. Only two of 12 weeks of the quarter were during ECQ.

A much higher rate of contraction is inevitable in the Second Quarter, perhaps -10% or more, as the period under quarantine is much longer. Some predict the annual decline for 2020 to be as severe as in 1984 and 1985 when it plunged by -7.3% each year. By 1986 growth resumed and remained steady for 43 years until this year, except for -0.6% in 1991 and also in 1998.

As presented in hearings in the House of Representatives of the Defeat COVID-19 Committee, the most vunerable sectors of the economy impacted by the quarantine include Construction, Land Transport, Retail Trade, and Tourism. Overall, the committee estimated the jobs of 23 milllion Filipinos are affected. Export manufacturers and BPOs are operating at reduced levels, while most garment export factories have stopped production as orders were cancelled. OFW remittances are projected to decrease 15-20%.

Like all countries, the Philippines faces the double challenge of flattening the COVID-19 curve, while simultaneously flattening the curve of a potential economic collapse. Both can have fatal consequences if not flattened.

The global economy is suffering with world trade possibly falling by one-third. Air travel has fallen by 95%. The United States, despite its resources, reports

[1] John Hopkins University School of Medicine, May 21, 2020

unemployment near 15%, the highest since the Great Depression. Almost 40 million Americans have applied for unemployment insurance since March;[2] unemployment skyrocketed from 4.4% to almost 20% in two months.

In such dire and challenging circumstances, the Congress faces a dual responsibility to provide for relief and stimulus to the population and to restore fiscal certainty to current and future investors, especially to foreign investors, during a period when major realignments of their Asian regional manufacturing footprint are underway.

In the four months since the above paragraphs were written, the pandemic and its economic impact have continued to destroy lives, jobs, and the confidence and hopes of not only the Philippines but the world as well. Virus positives now exceed 23 million people, and more than 800,000 deaths are reported.

The Philippines is learning to live with the virus until better treatment remedies and vaccines are widely available. The WHO has predicted the pandemic will end before the end of 2022. But the learning period of lockdowns - said to be the longest in the world - while saving many lives, has pummelled the economy, as shown in the GDP growth collapse of -16.5% in Q2 of 2020, the worst in the country's history. The result is severe contraction of major sectors, the loss of many millions of jobs, increased hunger and poverty, and weakened export markets.

Nevertheless, we can be optimistic and hope the famous Philippine resiliency will get the country through its current trials. As DOF Secretary Dominguez and BSP Governor Diokno have often pointed out, macroeconomic fundamentals are sound, with a strong currency, record international reserves, and a low debt-to-GDP ratio. We also compliment the legislators who have worked very hard to craft legislation to deal with immediate health and citizen support and business recovery requirements.

Two Myths Rebuted

In the July 30, 2020 slide presentation of DOF Asec. Labino, he presents three "myths" about CREATE.

Under Myth #1, the presentation states that in "2017, Php 441 billion in incentives were granted, many of which are redundant, to 3,150 firms." It continues to estimate the number of public markets, kilometers of roads, daycare centers, and classrooms this amount could have been funded had the incentives not been granted. These statements are extremely misleading. The DOF - an agency that is more focused on revenue generation than investment promotion - does not state how many direct and indirect jobs those firms created nor how much tax revenue the firms paid. Nor does it state that these firms had other choices to invest in than the Philippines, including Costa Rica, India, Malaysia, Mexico, South Africa, Thailand, Vietnam, and many others and that without these incentives most of the firms would not have invested in the Philippines. In other words, the investments actually resulted in jobs as well as revenue for public markets, roads, daycare centers, and classrooms. The firms came to the Philippines because of the quality of the country's workforce and the incentives offered, even though other costs of doing business (e.g. labor, logistics, security, utilities) were higher.

[2] Media reports, May 21, 2020

Under Myth #3, the presentation attempts to deny that the CREATE proposal has discouraged investments. The slide fails to explain the difference between "forever" investments and BOI investments. The former are for firms that compete in global markets. The later are usually awarded to domestic market firms, especially large infrastructure projects, such as the PRC steel mill ($3 billion), the Singaporean (PRC) fiberoptic cable project ($3 billion), and the New Manila International Airport project ($10 billion) (awarded in 2020 and not in the DOF table). More importantly, the table ignores the surveys of foreign investors in PEZA zones that revealed firms had stopped or reduced new investments precisely because of the DOF proposal made in December 2017 in TRAIN 2/TRABAHO/CITIRA, which proposed to raise taxes enormously on thousands of foreign investors who had been invited to invest in the Philippines under certain rules and now had been told by the DOF that the rules would change. Their reaction was to reduce new investments and wait and see, precisely because of the uncertainty created by the proposed law. A better slide would have shown the billions of US$ and tens of thousands of jobs from lost investments at PEZA, Clark, Subic, and other zones because the original DOF proposal made the country unattractive for many investors.

2. Vietnam, India*, and Indonesia*, are big winners from the shift away from China

Over the two decades since joining the WTO in late 2001, China has become the leading global manufacturer, attaining 25% of the global total with foreign investment of US$ 1.75 trillion from 2002 until 2018. Companies from Europe, Japan, Korea, Taiwan, and the US have been the leading investors in manufacturing in China. Starting with low technology products, such as apparel, appliances, footware, houseware, and toys, the sector rapidly transformed into more sophisticated products in automotive, electronics, railroad, semicondutors, shipbuilding, telecommunications, and others. Total exports grew rapdily from US$ 326 billion in 2002 to US$ 2.5 trlllion in 2019. According to offical statistics, there are 2.8 million factories in China.

China followed the well-known path to industrialization in Asia, as Japan and Korea did. In the last decade, foreign manufacturers began to diversify out of China. Reasons included rising production costs, especially for labor,[3] anti-Japanese riots, and intellectual property theft..More recently, the trend has intensified due to the US-initiated trade war with China, the call by governments of Japan, Korea, and the US for their multinational firms to reshore, and the COVID-19 crisis influencing firms to shift reliance on production bases in China to multiple international locations. As senior Home Depot executive Ted Decker stated in late 2019 "I am not aware of a single supplier who is not moving some form of manufacturing outside of China."

Vietnam has emerged as the country of first choice for international manufacturers moving production from China but not reshoring to their home countries.[4] The example of Samsung a decade ago with its huge investment in Vietnam is being followed by other large electronic contractors. Apple, whose products are assembled in China at 27 factories by nearly 1 million workers, is shifting some production to Vietnam, starting

[3] Manufacturing wages have risen eightfold since 2004.

[4] The Japanese, Korean, and American governments have policies to encourage their manufacturers to reshore manufacturing investments from overseas. Japan has created a $2.5 billion fund to assist companies to return.

in 2020 with 3 million of its wireless earbuds. Google is shifting production to Vietnam of its Pixel mobile phone and Home smart speaker.

Panasonic was reported to be closing its factory in Thailand to shift production to Vietnam, where it employs 8,000. The Nikkei report did not explain why the two factories in the Philippines were not included for additional workforce. Thousands of companies in light manufacturing are rushing to build factories in Vietnam.[5] We have to ask why aren't they rushing to the Philippines? The answers will guide policy corrections to prepare the Philippines to attract more relocating regional supply chain manufacturing. The new incentive package will be an important part of the policy corrections.

Nike lists 41 countries on its global manufacturing and sourcing map. Under Vietnam, the map shows 109 factories with 500,393 employees making apparel and footwear; this is 42% of the 1,164,201 workers that Nike indirectly employs at 533 factories globally. Although Cambodia, Indonesia, Malaysia, and Thailand also produce Nike products, the Philippines no longer does.[6]

Vietnam has managed the COVID-19 crisis extraordinarily well, with little impact on the health of its citzens. There have been no deaths and less than 300 persons infected. The country was the first in Southeast Asia to emerge from the pandemic after a lockdown of only three weeks, resume domestic flights, and expectations to retain its status as the region's fastest growing economy after 7% GDP growth in both 2018 and 2019. Its economy grew 3.8% in First Quarter 2020. Tourism arrivals (12 million in 2019) may take years to recover, while exports ($US 264 billion in 2019) are expected to fall due to weaker overseas markets but will increase as more foreign manufacturers move into Vietnam.

Prime Minister Nguyen Xuan Phuc told an audience of 6,000 at the largest-ever online business conference on May 9 that the growth target for 2020 is 5%, probably an over-optimistic goal. Vietnam reports approvals of US$38 billion in FDI in 2019, with Korea (US$7.9 billion), Hong Kong (US$7.9 billion), Japan (US$$4.14 and China (US$4.06 billion invested. Nikkei reported US$12.33 billion in FDI approved for January-April period 2020.[7] Not all of these proposed investments will be actualized but the high numbers indicate a very strong inward flow.

Vietnam has emerged from the pandemic as one of the least harmed economies in the world due to its immediate and thorough lockdown and effective testing, tracing, and treatment capability. With its economy less impacted, it is expected to continue to be the third largest recipient of FDI in ASEAN after Singapore and Indonesia. For the foreseeable future, analysts predict Vietnam will be the region's first choice for new

[5] various Nikkei articles in 2019 and 2020.

[6] www.nikemanufacturingmap.nikeinc.com

[7] Myanmar is another ASEAN member which escaped the pandemic with some 200 cases and 6 deaths, largely repatriations. Restaurants and schools are being permitted to re-open.

manufacturing locators moving out of China or seeking a regional site in addition to China.

AmCham has prepared a matrix comparing the Philippines and Vietnam on nearly 140 factors that foreign manufacturing firms may study when deciding between the two countries for an investment. Since Vietnam scores better overall, we suggest the matrix should be reviewed by appropriate Philippine government agencies and the Congress to review how the Philippines can compete better with Vietnam. (please see attachment)

India has launched a campaign to invite 1,000 American and other multinational manufacturing firms to relocate to India, according to recent media reports. A total area of 461,589 hectares has been identified by the government as available land area where the government will assist new locators who previously needed to acquire land on their own from small landowners.

Ten sectors have been prioritized – auto parts, chemicals, electronics, food processing, heavy engineering, leather goods, medical devices, pharmaceuticals, solar equipment, and textiles. The government's promotion agency Invest India is receiving inquiries from Japan, the U.S., South Korea and China, expressing interest to relocate to Asia's third-largest economy.

A special CIT rate of 15% is being offered to new foreign manufacturing investors. Companies availing of the 15% CIT may sell in the domestic economy (1.38 billion population). If they are export firms and locate in economic zones, they are entitled to an ITH. With over 120 million Indian citizens losing their jobs in recent months, India is campaigning to take full advantage of global manufacturing realignments as part of its economic recovery strategy.

India is having some initial successes in attracting large US companies. Apple partners have been producing inexpensive phones (including model 11) in India for the domestic market. But by mid-2011 the more advanced Model 12 wil be assembled in the country. Very recently Google announced it would invest US$10 billion in India over the next three years.

***Indonesia** has announced plans this year to seek more FDI aggressively. After winning his second term in office, President Joko Widodo announced plans for Indonesia to become not just a developed country but one of the world's largest economies by 2050. To get there the country will require massive investment, especially FDI. To achive this, refrms are needed, including lowering coporate income taxes, removing restricions on foreign investment, and relaxing labor restricions*

The government has designated a state-owned 4,000 hectare industrial park in central Java for new manufacturing locators. where the minimum monthly wage is $135. President Widodo has sent an ambiitous labor reform bill to the parliament intended to

lessen burdensome rules on employers and other legislation to liberalize business activities reserved for nationals.

On July 1, Widodo announced seven foreign firms had agreed to relocate facilities from China, totaling $850 million in new investment in Indonesia. The group included Panasonic (Japan) and LG Electronics (Korea).

The Philippines is not benefiting from the shift away from China and has yet to be seriously considered as an alternative to Vietnam, India, *and Indonesia.* BOI reports only a few dozen enquiries and a handful of firms deciding to relocate to sites in the Philippines.[8] Even if potential investors are aware of the advantages the Philippines offers, the fact they cannot calculate the changing tax environment because of the controversial TRAIN 2 legislation has discouraged new and expansion investments since first proposed in December 2017.

Surveys of Japanese investors in the Philippines conducted in 2018 reported most would downsize or depart the Philippines under the sharp increases in taxes originally proposed in TRAIN 2. The transition provisions in the succesive versions of the proposed legislation were considered insenstive and unwelcome by hundreds of previously satisifed Japanese businesses who had been prioritized in investment campaigns by successive administrations over four decades.

Present and potenial foreign investors of other nationalities reacted in similar fashion, and FDI in manufacturing, as measured by the Philippine Economic Zone Authority (PEZA), declined sharply from previous high levels. Foreign business chambers of commerce estimated severe jobs losses should the proposed law be enacted.

Fortunately, the SWMC committee report for CITIRA SB 1357 reduced these apprehensions of investment outflow and job destruction.

Then the COVID-19 pandemic struck and brought the exestential crisis of our lives.

3. CITIRA *(CREATE):* content and timing

Amidst these unprecedented circumstances of decreasing GDP, rising unemployment, and increasing competition for foreign investment, the Philippine Government plans to resume consideration of the CITIRA *(CREATE)* in the Senate and targets for the bill to achive final passage before the June 4 recess.

The undersigned see both positive and negative possibilities from completing the full legislation at this time.

Some have suggested to pass an updated version of the proposed Investment and Incentives Act of the Philippines that was extensively discussed but not approved in

[8] Media reports iof May 21, 2020 press conference of Undersecretary Ceferino Rudolfo.

the 16th and previous Congresses. However, the bill would have to be redrafted to take into account enhanced incentives for new investors in CITIRA (CREATE)[9] This suggestion has been repeatedly rejected over the last four years.

There is also the suggestion to pass the new DOF proposal to reduce the CIT to 25% beginning July 1, 2020 (or keeping the original January 1, 2020 effectivity date), while postponing passage of the Incentives Rationalization part of the bill until August to allow more careful consideration of its final contents.

Another option is to approve the CIT reform and section containing new incentives now and postpone approval of sections on exisiting investors until the second half of 2020. This would allow the BOI, PEZA, and other IPAs to offer the enhanced incentive menu to new investors sooner. The highly controversial treatment of existing investors would be studied further, in light of the impact of COVID-19 on their costs, markets, and prospects. Some of these companies are in intensive care and about to layoff workers and may close. During the lockdown, a significant number experienced production shifts to plants in other countries (Cambodia, Malaysia, Thailand, Vietnam.)

The **positive result of lowering the CIT to 25% would be to provide a "stimulus"** for the recovery of the economy by making more funds available for the country's one milllion firms to invest in employees and capital. DOF Secretary Dominguez has described this as "one of the largest ecnomic stimulus measures in the country's history." DOF estimates this reform would provide firms an infusion Php 625 billion to invest rather than pay to the government. We agree.

Another positive result of improving the fiscal incentives for new investors will be to **provide the Investment Promotion Agencies better incentives** as good as and better than those competing economies offer investors so that they invest more in the Philippines.nn

And enactment would end uncertainty created for many investors by more than two years of lengthy debate in Congress over controversial provisions of the legislation.

[9] Fiscal incentives rationalization was first proposed in 1995 as part of the comprehensive tax reform. However, it was not included in the resulting reform in 1997. Subsequent Congresses considered stand-alone bills entitled the Investment and Incentives Code of the Philippines, but the failure of DOF and DTI to agree left the status quo in place. For several IPAs – led by PEZA, CDC, and SBMA – the incentives attracted over 4,000 firms to locate employing more than 1 million Filipinos directly and creating some 5 million indirect jobs. Even a cost-benefit analysis of the cost and value of fiscal incentives as required to be done by NEDA under RA 10708 or TIMTA enacted in 2015 has not been completed and made available to Congress.

This uncertainty was the main reason for the decline in net FDI received by the Philippines in recent years, in contrast to Vietnam and others in SEA.[10]

However, while ending uncertainty should be overall positive for the country's investment climate, if existing investors face provisions that still degrade their financial projections - at a time when COVID-19 has harmed their operations – some will lose confidence in the Philippines as an investment location. We want existing investors to have increased confidence, decide to expand their investments, and confirm to firms considering investing in the Philippines that doing so is the right decision.

We encourage the Senate to approve the recommendation of the Department of Finance to <u>accelerate the CIT reduction to 25% effective July 2020</u> and continue reductions of 1% a year until reaching 20%. However, <u>we recommend that the reduction continue at one year intervals in order to reach 20% in 2025 rather than in 2027</u>. Under the CREATE proposal the Philippines will still retain the highest CIT rate in Southeast Asia until 2027. The CREATE proposal is to remain at 25% for 2020, 2021, and 2022 before decreasing to 20%.

> **Indonesia**, which had a 25% CIT when TRAIN 2 was proposed, has reduced its CIT to 22%, to be followed by another reduction to 20% in two years. *Indonesia also is offering a CIT as low as 17% to the more than 600 firms that are listed on the Jakarta Stock Exchange.*
>
> **Vietnam** is discussing to cut its CIT and VAT on SMEs by 50%. The current proposal is to reduce the CIT from 20% to 10% for SMEs (compared to 30% currently in the Philippines and 20% in 5 years as proposed by CREATE.)

The <u>critical issue for the undersigned with the proposed legislation is whether in its present form CITIRA (CREATE) will benefit or harm current investors</u>, who are experiencing the unexpected effects of the quarantine period and depressed operating conditions.

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[10] Table: FDI inflows, ASEAN-6, 2009-2019

	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019*	Total
Total ASEAN	41.4	113.0	86.0	112.1	118.2	129.4	114.3	116.8	144.2	148.7	177.0	1 301.1
Indonesia	4.9	13.8	19.2	19.1	18.8	21.8	16.6	3.9	20.6	22.0	24.4	185.1
Malaysia	1.4	9.2	12.0	9.4	12.1	10.9	10.2	11.3	9.3	8.1	9.0	102.9
Philippines	2.0	1.3	1.8	2.8	3.9	5.8	5.6	8.3	10.3	9.8	7.6	59.2
Singapore	18.9	57.2	39.9	60.1	56.7	73.3	59.7	73.9	75.5	77.6	105.4	698.2
Thailand	6.4	14.7	2.5	12.9	15.9	5.0	8.9	2.8	8.2	13.2	13.7	104.2
Viet Nam	7.6	8.0	7.5	8.4	8.9	9.2	11.8	12.6	14.1	15.5	16.1	119.7

* 2019 Forecasts from UNCTAD except for Philippines. Actual 2019 PH data from BSP.
Actual data from BSP (Philippines) and CEIC (Indonesia, Malaysia, Singapore Thailand, and Vietnam)
BSP FDI data and UNCTAD data may vary, as they did in 2018 when BSP reported $9.8 billion and UNCTAD reported $6.5 billion

During *over five months of* quarantine *export industry* investors have experienced displacement of workforce to work-from-home, addiitonal costs for accommodations near factories and at worksites, expenses for shuttle transport for employees who could not use pubic transportation, payment of salaries for employees who could not work, loss of overseas orders due to cancellations, and shift of overseas orders to other regional plants that were more productive, delays in arrival of raw material imports due to port delays due to inadequate BOC staffing, and other reasons.

*The **business process outsourcing industry** is considered as one of the country's largest job generators and one of its biggest private sector employers, creating jobs for 1.3 million Filipinos and indirectly impacting close to 4.2 million jobs in other industries across the country. Alongside OFW remittances and tourism receipts, the IT-BPM industry is one of the economy's major sources of foreign exchange with recorded revenues of USD26.3 Billion by end of 2019, fueling the Philippine economy.*

While a majority of the IT-BPM workforce is able to render essential services to domestic and international clients throughout the Community Quarantine, the industry is not quite Business As Usual yet. Given the unprecedented consequences of Covid-19, the sector is facing strong headwinds - with reduced revenues arising from reduced productive capacity, and significant increase in expenses to enable continuity of operations (i.e. provision of food and lodging, shuttle services, massive Work-From-Home enablement, etc.). Being one of the only few industries that continued to persevere during the Community Quarantine, it is imperative for the Philippines and the IT-BPM industry to remain agile amid the changing landscape.

For example, one large BPO company which employs 5,000 pays Php 1 million a month for shuttle service. DTI and DOLE now reuire that shuttle service must be provided for companies with assets above Php 15 million.

Another BPO company had to move 20,000 CPUs from office to WFH in five days in March.

***Electronic exporters** experienced orders being shifted to other plants in Southeast Asia because operating costs went up in the Philippines. The industry expects exports in 2020 to decline by 23%.*

The cost to house 1,000 workers in a hotel near a worksite is at least Php 1,500 a day and Php 30,000 a month for 20 days, amounting to Php 30 million. Such housing was required for many firms during the ECQ.

These costs are rapidly adding up for export companies, as they are for domestic market companies. As the cost of operating in the Philippines increases, companies will decide to shift some production abroad. Even domestic firms may be harmed by

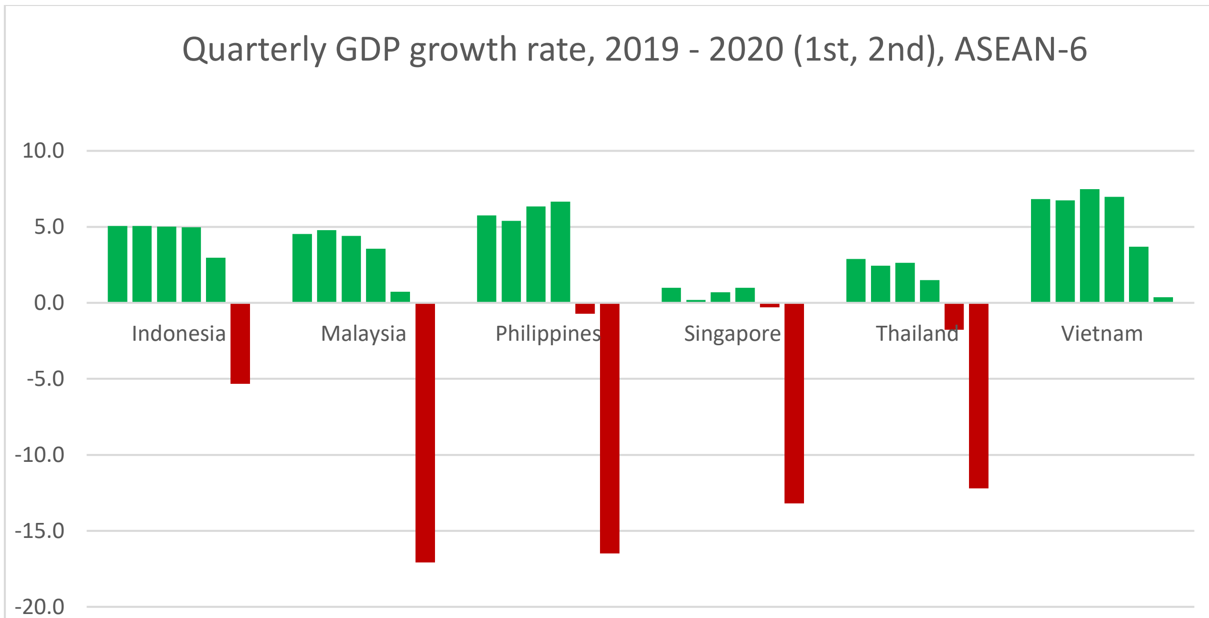
cheaper imports from Vietnam, where firms do not have to pay comparable local pandemic-related costs.

***Garment export firms** are left with no choice but to lay off employees by thousands. They are struggling to have orders, mostly losing more than half of orders, others in a worst situation of having no orders, repeat no orders at all. Demand for new clothing and other wearables has collapsed in major markets in America and Europe. Some factories shifted to making PPEs for the domestic market, but, as reported in the media on August 22 and 23, government procurement offices are still buying from China. Fortunately, CREATE allows "footloose" companies to keep their 5% GIE tax. However, even this benefit will not help if they shut down. Not long ago over a million Filipinos worked in the garment export industry. Today, the future of the industry is bleak.*

Export statistics for wearables show that both apparel and travel goods have been badly hit, for Jan-June 2020 both exports went down by 44% and 43% respectively. (Travel goods include products such as luggage, backpacks, travel/sports bags, business cases/computer bags, handbags, personal leather goods, and luggage locks).

Noting the current trend, the industry association projects between -40 to -50% for wearables for 2020 and, if the same conditions exist, recovery won't be seen soon and 2021 would experience -25 to -30% loss.

The sharp contraction in GDP growth in Q2 2020 (see figure below) indicates the entire year 2020 will be negative. Estimates are in the -4% to -7% range, with NEDA at -5.5%. The next few years should see positive growth but probably not as high as pre-pandemic. Global export markets are likely to remain depressed, as will OFW remittances, domestic demand, and tourism sector revenue. Among the ASEAN-6 economies, only Vietnam is expected to have positive GDP growth in 2020.



Source: CEIC

The table below shows actual and estimated export value for the period 2017 to 2022 for three export sectors that have been well-established in the Philippines as a result of past fiscal incentives: (1) garments, (2) business processing services, and (3) semiconductors and electronics.

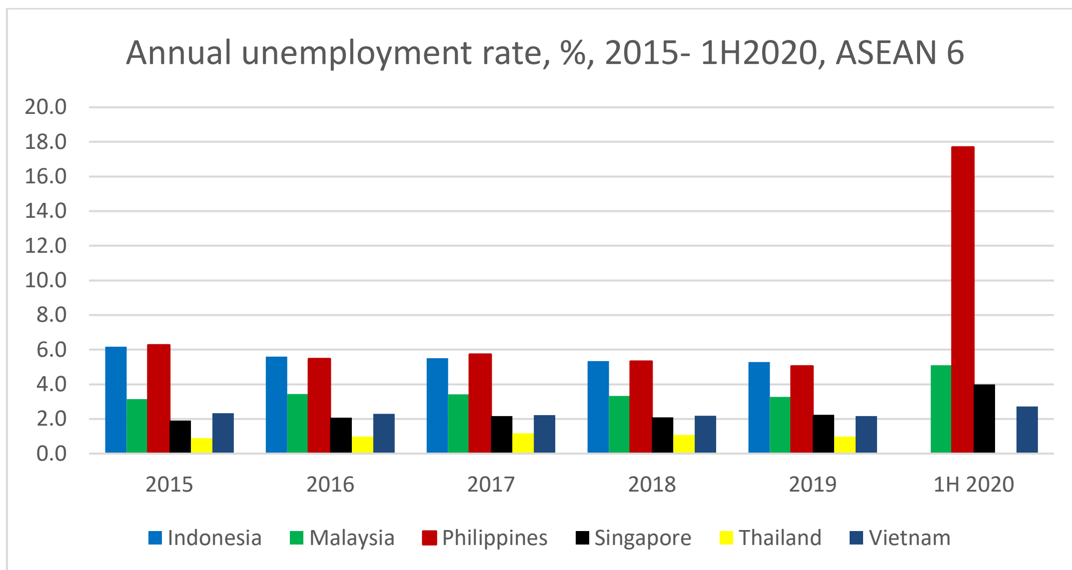
Exports of Garments, IT-BPO, and Semiconductors from 2017 to 2021 (in US$ billion)

	2017	2018	2019	2020 (industry estimate)	2021 (industry estimate)
Garments[1]	1.7	1.6	1.8	1.0 (0.5 actual exports for YTD Jan-June 2020)	0.7
IT-BPO[2] [3]	23.4	24.5	26.3	28.0*	30.0*
Semiconductors	36.5	41.6	43.3	33 (17.1 actual exports for YTD Jan-June 2020)	35

[1] Total for apparel, travel goods, and footwear
[2] Reflects total IT-BPO industry revenue, not just export revenues
[3] IT-BPO estimates for 2020 and 2021 are pre-COVID projections

Sources: CONWEP, IBPAP, and SEIPI

Negative economic growth and lockdowns have resulted in extensive job losses, as shown in the figure below (data from Indonesia and Thailand is not yet available). It appears the Philippines will experience the worst job loss of the ASEAN-6 economies.



Source: CEIC

4. SB 1357: comments, proposed rewording, and amendments

Summary of fiscal incentive recommendations for 4 types of investor

Overall request: retain the existing tax incentives for at least **five years** and then apply new incentives rules:

1.a Existing investors on ITH and GIE

- Additional two years of ITH
- On GIE, retain existing tax incentives for five (5) years, after which sunset rules apply

1.b Sunset Rules (Transition Period)

- If on ITH, complete the ITH ***(included in CREATE)***
- Sunset of 4, 5, 7 years (rather than 2-3-5-7 in CITIRA) ***(included in CREATE)***
- After sunset ends, regular CIT applies or eligible for conditional grandfathering, i.e., 5% GIE to continue provided that any of the conditions are maintained, namely, 90% exporter, 10k employees, and footloose

2. New investors

- ITH for variable periods followed by CIT ***(included in CREATE)***
- Investors supplying domestic markets eligible for incentives
- Increase maximum period of ITH from 12 to 20 years for approved new domestic and foreign owned investments in less developed areas
- Special CIT on gross income of 8% (2021), 9% (2022), and 10% (2023) in lieu of national and local taxes ***(included in CREATE)***
- Maintaining any of the conditions 90% exporter, 10K employees, and footloose 5% GIE
- Enhanced deductions ***(included in CREATE)***

3. ROHQs

- Subject to 10% of taxable income provided that after 5 years existing ROHQs shall be subject to regular CIT
- Add other relevant and competitive incentives package for qualified employees

4. All others

- CIT of 25% starting January 1, 2020, 1% decrease until January 2025 to reach 20% CIT
- Microenterprises with assets below P3M CIT of 10% on taxable income after 2 year ITH under BMBE law
- For small enterprises with assets between P3M and P15M CIT of 15% on taxable income
- For medium enterprises with assets between P15M and P100M CIT of 20% on taxable income
- Suspend 2% Minimum Corporate Income Tax (MCIT) for 5 years
- 300% additional R&D expense deduction from gross income
- tax credit (1% of gross revenue or gross receipts using e-invoicing) for IT infrastructure expenses to enable use of computerized accounting system

Detailed recommendations follow.

Section 3 amending Sections 4 of the NIRC – (on Power of Secretary of Finance to Interpret Tax Incentives)

We suggest the deletion of the proviso granting the Secretary of Finance the exclusive and original jurisdiction to interpret the provisions on the tax incentives. We believe that such power should be left to the Investment Promotion Agency (IPA) tasked by the legislature to implement the intent of this bill, i.e., to attract foreign investments.

We note that even if the power to interpret tax incentive provisions is left with the IPAs, it will not preclude the Bureau of Internal Revenue (BIR) from challenging the interpretation and going to court. Foreign investors need assurance that incentive laws will be interpreted according to their intent and spirit and not according to "its letter that killeth." Foreign investors have many choices of where to invest and are discouraged by too many level of bureaucratic approvals. This power also seems contrary to the Ease of Doing Business reform of the Duterte Administration, which was intended to reduce the burden of regulatory approval. The FIRB may conduct oversight of IPAs and correct what might be determined to be misapplications of incentives.

Sections 5 and 6 amending Sections 27 and 28, respectively, of the NIRC Reduction of Corporate Income Tax Rate

Our suggestion is to revise Section 27 and 28 to read, as follows:

> *"SECTION 27. Rates of Income Tax on Domestic Corporations. —*
>
> *"(A) In General. — Except as otherwise provided in this Code, beginning **January 1, 2020**, an income tax of twenty-five percent (25%) is hereby imposed upon the taxable income derived during each taxable year from all sources within and without the Philippines by every corporation, as defined in Section 22(B) of this Code and taxable under this Title as a corporation, organized in, or existing under the laws of the Philippines: Provided, That the rate of corporate income tax shall be twenty four percent (24%) beginning January 1, 2021; twenty three percent (23%) beginning January 1, 2022; Twenty two percent (22%) beginning January 1, 2023; Twenty one percent (21%) beginning January 1, 2024 and **Twenty percent (20%) beginning January 1, 2025**.*
>
> ***Micro enterprises** with asset size of Php 3 Million or less shall be subject to 10% of taxable income from all sources after the expiration of their income tax holiday of two years under the BMBE Law; Small Enterprises with asset size of more than Php 3 Million but not more than Php 15 Million shall be subject to 15% on taxable income from all sources; while Medium Enterprises with asset size of more than Php 15 Million but not more than Php 100 Million shall be subject to 20% of taxable income from all sources."*

"SECTION 28. Rates of Income Tax on Foreign Corporations. —

(A) Tax on Resident Foreign Corporations. —
(1) In General. — Except as otherwise provided in this Code, beginning ***January 1, 2020****, a corporation organized, authorized, or existing under the laws of any foreign country, engaged in trade or business within the Philippines, shall be subject to an income tax of twenty-five percent (25%) of the taxable income derived in the preceding taxable year from all sources within the Philippines: Provided, That effective January 1, 2021, the rate of income tax shall be twenty four percent (24%); twenty three percent (23%) beginning January 1, 2022; Twenty two percent (22%) beginning January 1, 2023; Twenty one percent (21%) beginning January 1, 2024 and Twenty percent* ***(20%) beginning January 1, 2025****."*

Small Enterprises *with asset size of more than Php 3 Million but not more than Php 15 Million shall be subject to 15% on taxable income from all sources; while Medium Enterprises with asset size of more than Php 15 Million but not more than Php 100 Million shall be subject to 20% of taxable income from all sources."*

We believe that our corporate income tax rates must also be equitable, that is, based on one's ability to pay as mandated by the Constitution. We note most ASEAN countries do not follow the single tier of corporate taxation because simple logic will tell us that it is not equitable.

You can readily verify that Indonesia only applies 50% of their regular CIT (22% beginning 2020) to their SMEs with gross turnover of not more than Php 170.4 Million. In Thailand, companies with paid up capital of not more than Php 7.9 Million and with gross turnover of not more than Php 47.4 Million are subject to progressive CIT rate of 0%, 15% and 20%. Beginning 2019, Malaysia subjects only to 17% CIT the first Php 23 Million of taxable income and the balance to 24% CIT. In Singapore, 75% of the first Php 356,000 of taxable income is exempt from CIT, and only 50% of the next Php 6.7 Million of taxable income is subject to 17% CIT, the balance of taxable income is subject to 17% CIT *(Source: 2019 Ernst & Young Worldwide Corporate Tax Guide, fx conversion using US$50.68/US$1.00)*.

Further, Vietnam is considering reducing the current 20% CIT rate to 10% for SMEs.

Accordingly, the provisos in Section 34 (B)(1) of the NIRC should also be revised to read, as follows:

"Section 34. Deductions from Gross Income. xxx
(A) Expenses
(B) Interest. - xxx
(1) In General. –

Provided, however, that the taxpayer's otherwise allowable deduction for interest expense shall be reduced by 20% beginning ***January 1, 2020;*** *Provided, Further, that the following percentages shall apply if the corporate income rate as provided in Sections 27 (A) and 28 (A)(1) is adjusted:*

(a) If rate is twenty four percent (24%), interest rate reduction is sixteen percent (16%);
(b) If rate is twenty three percent (23%), interest rate reduction is thirteen percent (13%);
(c) If rate is twenty two percent (22%), interest rate reduction is nine percent (9%);
(d) If rate is twenty one percent (21%), interest rate reduction is five percent (5%);
(e) *If rate is twenty percent (20%), interest rate reduction is zero percent (0%)."*

We strongly recommend that the above rate reduction in CIT be made retroactive to January 1, 2020, so that companies particularly SMEs will immediately get reprieve from onerous taxation.

Equally crucial, the **2% Minimum Corporate Income Tax (MCIT)** should also be **suspended for all companies for a period at least five (5) years** as we expect that most corporate taxpayers will be in tax loss position given the tremendous economic loss brought about by Covid-19 which will certainly still be felt in coming years. We believe the proposal to extend NOLCO from 3 to 5 years will become a token benefit, unless the MCIT will be suspended as well for the same period.

Along with the proposal to extend net-operating loss carry-over (NOLCO) to 5 years, we are also **proposing a 300% additional research and development (R&D) expense** (similar to Indonesia and Hongkong) as deduction from gross income to encourage innovation, technological and digital transformation among companies.

We also believe that the government should revive the proposal of granting of **tax credit (1% of gross revenue or gross receipts using e-invoicing) to companies for IT infrastructure expenses** to enable the use of computerized accounting system and/or e-invoicing. This will immensely help the BIR's effort to implement e-invoicing under TRAIN 1.

We also recommend that **Section 32 (B) (4) of the NIRC be amended** to read, as follows:

"Section 32. Gross Income.

xxx xxx

(B) Exclusions from Gross Income. — The following items shall not be included in gross income and shall be exempt from taxation under this Title:

xxx xxx

(4) Compensation for Injuries or Sickness and compensation during prolonged state of national emergency. — Amounts received, through Accident or Health Insurance or under Workmen's Compensation Acts, as compensation for personal injuries or sickness, plus the amounts of any damages received, whether by suit or agreement, on account of such injuries or sickness. Any amount of compensation, salary, benefit and/or financial assistance, in cash or in kind, provided to employees during prolonged state of emergency, calamities, pandemic, national epidemic or any force majeure shall not be subject to income tax."

Section 6 amending Section 28 (A)(5) of the NIRC – (on BPRT Exemption of PEZA Philippine Branches)** **(Included in CREATE)

We recommend the retention of the exemption from Branch Profit Remittance Tax (BPRT) of PEZA-registered Philippine Branches so they can reinvest their profits for further expansion in the Philippines.

***Section 6 amending Section 28 (A)(6)(b) of the NIRC* – (on ROHQs)**

We reiterate our recommendation to rephrase the above provision, as follows:

> *"Regional Operating Headquarters as defined under Section 22 (EE) shall pay a tax of ten percent (10%) of their taxable income: Provided, that after **five (5) years** from the effectivity of this Act, existing regional operating headquarters shall be subject to the regular corporate income tax; provided, further, that the SIPP shall include in the list of qualified activities those covered in Section 22 (EE) of the National Internal Revenue Code which shall henceforth be provided by Global Corporate Centers (GCCs); Provided, Further, that those that will qualify as GCCs under the conditions stipulated in the SIPP shall continue to be taxed at ten percent (10%) of their taxable income, for the periods to be provided under the SIPP but in no case to exceed eight (8) years from the effectivity of this Act; provided, finally, that GCCs may be a domestic or foreign corporation."*

As many ROHQs serve mostly foreign affiliates, we believe that the shared services industry should be encouraged by allowing them to avail of the incentives under this bill, if they are so qualified.

We request your good office to carefully consider the important points extensively discussed in the position paper of the Philippine Association of Multinational Companies' Regional Headquarter, Inc. (PAMURI) regarding the importance of the shared services sector as a rising industry. At this time of extraordinarily high unemployment and uncertainty about future job prospects, the government should

avoid actions that may lead to the closure of such firms and the loss of jobs to competitors described below.

We believe that it is also very important for your Committee to know that Thailand and Malaysia continue to provide incentives to their ROHQs and have tailored them in a way that their ROHQs are compliant with the OECD guidelines against "harmful tax practices." Thailand, in particular, now grants a preferential corporate income tax of 3%, 5% or 8% (and 15% personal income tax on expatriate employees) to their **International Business Centers** (IBCs, their equivalent of ROHQs) depending on the amount of local expenditure of the IBC. We believe that the same can be done in the Philippines to encourage the growth of the shared services industry.

As we noted above, Thailand is able to maintain its 15% preferential income tax at least for its expatriates and has passed the OECD peer review despite maintaining it. In the post-Covid world, where the Philippines is facing very stiff competition in the region. We believe that the incentives for regional offices should continue to be encouraged and incentivized. The same policies should be adopted that will entice regional offices to locate in the Philippines, benefitting the country in the long run in terms of technology transfer on business and management processes and bringing about increased economic and consumer activity,

Section 9 introducing new Section 294 of the NIRC – (on Allocation of Revenue between IPAs and LGU)

We strongly recommend that the bill should already provide the exact respective percentage share of the IPAs and LGUs in the special corporate income tax rate that will be paid by the Registered Business Enterprises (RBEs). Otherwise, this will become a contentious issue later on.

<u>On Incentives, in General</u>

We express grave concern on the Department of Finance's (DOF) proposal to "tailor fit" incentives. This will further aggravate the feeling of uncertainty and apprehension from foreign investors as they do not know what incentives they will be able to negotiate from the government. On the other hand, the idea of "tailor fitting" of incentives can greatly complement the government's effort to attract FDIs if the tailor-fitted incentives are in addition to the minimum set of incentives that will be set by either CITIRA or CREATE.

Thus we express our strong clamor to <u>retain the existing tax incentives for a period of at least five (5) years</u> to arrest this lingering doubt and ambiguity in government's policy about tax incentives vis-à-vis attracting FDIs.

We also cannot overemphasize our unequivocal support to PEZA and its one stop shop to be maintained as the leading investment promotion agency for exporters in our

PEZA industrial zones and ecozones. For nearly two decades, PEZA's highly professional, corruption-free, and dedicated staff has served thousands of very pleased and appreciative investors.

After maintaining the status quo for at least five (5) years, we believe that the following suggested refinements will aid in the execution of the tax incentive provisions of SB 1357:

In recogntion of the hardship of incentivized firms of the quarantine and weaker GDP growth, provide firms currently receiving ITH with an additional two years of ITH

New Section 294

We are recommending to add another proviso to Section 294 B) that will read, as follows (please see underlined proviso)

> *"Sec. 294. Incentives. – subject to the conditions and period of availment in sections 295 and 296, respectively, the following types of tax incentives may be granted to registered projects or activities:*
> *(A) Income Tax Holiday;*
> *(B) Special Corporate Income Tax Rate - A tax rate equivalent to eight percent (8%) effective January 1, 2021, nine percent (9%) effective January 1, 2022, and ten percent (10%) effective January 1, 2023 onwards, based on the gross income earned, in lieu of all taxes, both national and local, as specified in the respective special laws of the investment promotion agencies: provided, that, the National Government share shall be as follows: six percent (6%) in 2021, seven percent (7%) in 2022 and eight percent (8%) in 2023 onwards: Provided Further, that, if applicable, the shares of the local government units and the investment promotion agencies under the special laws governing the latter shall be observed; Provided Finally, that for RBEs that qualify under any of the condtions under subsections (i), (ii), and (iii) of section 311, the applicable GIE tax rate shall be five percent (5%), the entitlement to which shall be subject to the same condition as that imposed in the last paragraph of Section 311.*

The rationale of the proviso is to make the Philippines more attractive to potential foreign investors who are going out of China while recognizing the government's effort to make the granting of tax incentives to become time-bound and targeted as the 5% GIE can only be enjoyed by new RBEs if they are able to maintain any of the conditions in Section 311 subsection i to iii, i.e. exporting 90% of their output; will employ 10,000 employees; or comply with the conditions for a footloose activity.

New Section 294 (C)(2) to (7) and Section 295 (B) – (on Enhanced Deductions)

We recommend to delete the phrase “up to” to get rid of the uncertainty and eliminate the exercise of discretion by the approving body. For example, if the training is already approved by the IPA, why does the FIRB need to determine the allowable percentage of deduction for such training? This will make everything too bureaucratic and opposed to the government’s goal of simplifying doing business in the country.

New Section 294 (C)(7) and Section 295 (B)(7) – (on Investment Allowance)

We believe that reinvestment allowance should not be limited to the manufacturing industry. The reinvestment allowance should be applied to all registrable industries to encourage expansion projects of foreign investors in the country and generate the much needed high-paying jobs that our countrymen need to grow the middle-class segment of our society.

New Section 295 (B)

We suggest to reword the first sentence of Section 295 (B) to read, as follows:

> *“At the option of the newly registered business enterprise, the enhanced deductions shall be granted in lieu of the income tax holiday and the special corporate income tax rate;”*

The underlined phrase will provide clarity that the availment of the enhanced deduction is an option of the applicant/registrant. We note that as Section 295 (B) is currently worded now, it is not clear if the RBE has the option to avail of the enhanced deduction instead of the ITH or SCIT.

New Section 295 (B)(4) – (on Approval of Trainings by IPAs)

We do not see the need for approval of the trainings by IPAs. The IPAs cannot claim that they know better which trainings are necessary and indispensable to the operations of the RBEs. Prior approval of trainings by IPAs will just add to the bureaucratic process. In the alternative, if prior approval by IPAs of trainings will be required, then, all trainings should be allowed 200% additional deduction already without need of any further conditions anymore.

New Section 295 (C)(1) – (on Conditions for Duty-Free Importation)

We suggest to remove the conditions that the imported capital equipment, raw materials, and spare parts are not produced or manufactured locally in sufficient quantity or of comparable quality and at reasonable price. We believe that these are useless conditions given that additional domestic input expense should be enough to encourage local sourcing of supplies by RBEs.

***New Section 295 (C)(2)(d)– (on Subsequent Dispositions of Capital Equipment, etc*) **(Included inJuly 30 version of CREATE)**

We strongly recommend to add a proviso in Section 295 (C)(2)(d) that will read, as follows:

> *"(d) Proven technical obsolescence of the capital equipment, raw materials, spare parts or accessories.*
>
> *Provided that, transfer by donation of machinery, equipment, raw materials, spare parts or accessories to TESDA, state colleges and universities, or DECS/CHED-accredited schools due to technical obsolescence shall be exempt from duties and taxes, including donor's tax.*
>
> *All transfers that comply with the aforementioned conditions enumerated in (a), (c) and (d) above shall not result to the imposition of the taxes not imposed upon tax and duty-free importation of the said capital equipment, raw materials, spare parts, or accessories."*

The proviso is meant to facilitate the donation of equipment particularly computers and laptops to schools that will enhance the learning of both students and teachers. Currently, such donations are required to pay duties and taxes based on original cost, resulting in few donations.

The last paragraph is meant to provide clarity that transfers that comply with the above conditions will not be subject to duties and taxes.

New Section 295 (D) VAT Exemption on Importation and VAT zero-rating on Local Purchases

We recommend that the said new Section 295 (D) be reworded, as follows:

> *"Sec. 295. Conditions of availment. - the tax incentives in the preceding section shall be governed by the following rules*
>
> *(d) The VAT exemption on importation andVATt zero-rating on local purchases shall apply to all purchases of goods and/or services by registered business enterprise located inside an ecozone or freeport."*

We are suggesting the deletion of the requirement that the purchase must be directly and exclusively used in the business of the locator since the latter will most likely not have any activities subject to 12% VAT. Hence, any accumulation of input taxes for purchases of services like security services, legal, and accounting services, etc. will mean trapped cash for the locator and requiring them to file a claim for refund for those unutilized input will only mean added bureaucracy and business cost for the locators which are all unnecessary.

New Section 296 (A), 2nd Proviso – (on SCIT for Existing RBEs)

For clarity, we recommend that the second proviso be reworded to read, as follows:

> *"That existing registered projects or activities prior to the effectivity of this Act may qualify to register under this Act and avail of the special corporate income tax or enhanced deductions for the prescribed period subject to the criteria and conditions set forth in the Strategic Investment Priority Plan. The SCIT for existing registered projects or activities, if availed of, shall not exceed twelve (12) years."*

The underlined statement will provide clarity that the SCIT for existing registered RBEs or activities can also be up to 12 years and that the Enhanced Deductions can also be availed of by existing RBEs. We note that it is not clear in the current wording of this provision if existing RBEs can also avail of the Enhanced Deductions.

New Section 296 (B) – (on Location Criteria)

Increase the maximum period of **the ITH from 12 to 20 years**, at the discretion of the responsible IPA, for approved new domestic and foreign owned investments in less developed areas in support of the *Balik Probinsya* program under EO 114 in order to address overpopulation, traffic congestion and pollution in Metro Manila.

We recommend that the **location classification be revised** to read, as follows:

> *"(1) NCR and Metropolitan Areas defined as… xxx;*
> *(2) Areas adjacent to NCR (Bulacan, Cavite, Laguna and Rizal);*
> *(3) Less Developed Areas (LDA) and All Other Areas."*

We believe that what should be considered as "Metropolitan Areas" must be clearly defined to avoid confusion.

We believe that the above classification is more attuned with the government's aim of promoting countryside development towards increasing inclusive growth.

New Section 297 and all of the provisions related to FIRB

Consistent with our proposal to maintain the status quo for five (5), we are recommending the activation of the Fiscal Incentives Review Board (FIRB) and all of the provisions related to its expanded functions only **after 5 years**, so that the country can respond quickly and efficiently to potential foreign investors who are refocusing their supply chain out of China.

Definitely, this is not the time to experiment and transfer the power and functions of existing efficient IPAs like PEZA to a body that has no proven track record, much less,

experience. We need to be agile and efficient at this point when companies are scrambling to move out of China. We take note that replacing the IPAs now with the FIRB will require so much time and effort to recalibrate and establish new processes for evaluation and approval of investments. Foreign investors will not wait for us as they would like to recover their lost time and income due to Covid-19.

New Section 297 (B) – (on the Expanded Functions of the FIRB)

In relation to the expanded functions of the FIRB, if and when it is convened, we propose that Section 297 (B) be reworded, as follows:

> *"Section 297. Expanded Functions of the Fiscal Incentives Review Board. –*
>
> *(A) xxx xxx*
>
> *(B) To approve or disapprove the grant of tax incentives but **only for investments exceeding US$ 500 Million**, upon recommendation of the Investment Promotion Agency: Provided, that the application for tax incentives shall be deemed approved if not decided upon by the FIRB after twenty (20) days from submission of the Investment Promotion Agency's recommendation to the FIRB: xxx"*

We believe that the role of the FIRB should not be so broad as to approve all grants of incentives but limited to those that are the largest and major projects exceeding US$ 500 million in capital.

New Section 304 (Qualifications of a Registered Business Enterprise for Tax Incentives

We take note that Senate Bill No. 1357 only clearly provides (in Section 296 (A) and in Section 311 (C)) that existing RBEs, upon effectivity of this Act, only have the OPTION to DEREGISTER and then, register under this Act and will only be entitled to SCIT as an incentive.

We wish to bring to your attention that SB 1357, even if read in its entirety, is still not clear if existing RBEs can register their expansion activities or renew their incentives, if qualified, after their pertinent incentives expire. In other words, there is nothing in SB 1357 that explicitly states that existing RBEs can register their expansion activities or renew their incentives when they expire. We respectfully emphasize that these benefits, namely, registration of expansion activities and renewal of incentives, were repeatedly promised to the private sector both by Cong. Salceda and Usec. Chua in various fora.

Thus, to avoid confusion and make sure that this commitment of the government will be realized, we are recommending to **add a new paragraph *F* to Section 304** that will read, as follows:

> *"Section 304. Qualifications of a Registered Business Enterprise for Tax Incentives. - xxx xxx xxx*
>
> *(F) Expansion Projects and Renewal of Applications.*
> *Expansion of registered activities existing upon approval of this Act may qualify to register under this Act and will be entitled to five (5) years of ITH and five (5) years of 5% GIE thereafter. Renewal of expiring registered project or activities approved before this Act and expansion projects of new RBEs approved under this Act shall be entitled to applicable incentives under Section 294 for the prescribed period subject to the criteria and conditions set forth in the Strategic Investments Priorities Plan"*

We believe that giving the registrants the opportunity to register their expansion activities or renew their expiring incentives will further encourage foreign investment into the country and would still be in keeping with the government's aim to make the incentives time-bound and performance-based.

Chapter VI Transitory and Miscellaneous Provisions

New Section 311

We are strongly proposing that new Section 311 be revised to read, as follows:

> *"Section 311. Investments Prior to the Effectivity of this Act.*
>
> *Registered Business Enterprises with incentives granted prior to the effectivity of this Act shall continue to enjoy their respective incentives for a period of five (5) years;*
>
> *(a) During the five-year period, RBEs whose projects or activities are under ITH will continue to enjoy their unexpired ITH as specified in the terms and conditions of their registration; and*
>
> *(b) RBEs whose ITH will expire within or after the above five-year period and RBEs currently availing of the five (5) percent tax on gross income earned granted prior to the effectivity of this Act shall be allowed to continue under the 5% GIE incentive; and after the said 5-year period, in accordance with the following schedule;*

1) *Four (4) years for projects or activities availing of the 5% GIE for more than ten (10) years;*
2) *Five (5) years for projects or activities availing of the 5% GIE for ten (10) years or less but for more than five (5) years; and*
3) *Seven (7) years for projects or activities availing of the 5% GIE for five (5) years or less.*

However, existing projects or activities who are under the ITH or 5% GIE incentive after the said 5-year period will maintain their 5% GIE incentive even after the above schedule expires provided that they satisfy any of the following conditions:

i. *Registered exporters that export ninety percent (90%) of their goods and/or services;*

ii. *RBEs that employ at least ten thousand (10,000) Filipino employees directly engaged in the production of the registered project or activity prior to the effectivity of this act; or*

iii. *Registered enterprises engaged in footloose projects or activities as defined herein.*

The entitlement to the 5% GIE will be subject to the RBEs continuing to meet any of the aforesaid conditions."

The maintenance of the five-year period above is being asked considering the unprecedented severe business losses incurred and still being incurred by exporters due to Covid-19. All leading economists are telling us that it will take years for the country to recover. Coupled with the fact that no reliable vaccine is on the horizon yet, we believe it is but reasonable and logical to let the dust settle first (and we do not know yet when it will settle) and give existing investors a period of 5 years before any drastic changes in tax incentives are put in place.

As you are very much aware, in 2019, the global economy was unsettled by the disruptive US-China trade dispute. In recent months, the Philippines experienced a volcanic eruption in proximity to many of the country's largest export industrial estates.

Soon thereafter (COVID-19) arrived. The world and the Philippines began a global lockdown which has completely shattered expectations of economic growth as well as our lives, as we knew them, until science develops treatment and vaccines. There is no guarantee that sciience will succeed soon or that the new medicines will be available in the Philippines even within the next 12 months. And with the crowded living conditions facing many millions of Filipinos living in extreme poverty in large cities successive waves of the pandemic cannot be ruled out despite the best efforts of the

government to protect the people and the economy. Already, the WHO has warned governments in Southeast Asia that they may be relaxing their restictions too soon.

The uncertainty created since late 2017 for existing foreign investors availing of fiscal incentives by the proposed TRAIN 2/TRABAHO/CITIRA tax regimes led to significant reductions in inward FDI in PEZA and other major special economic zones. Billions of dollars and tens of thousands of new jobs from new investors and expansion projects were lost.

Trade uncertainty between the world's two largest economies and the pandemic are leading to large realignments of regional logistics supply chains as the reliance of multinational firms on manufacturing in China is being questioned, leading to accelerated diversification out of China into Southeast Asia, especially Vietnam.

Unfortunately, the Philippines is not benefiting with increased inward FDI due to the policy uncertainty over the last two years over the future of fiscal incentives. The uncertainty was created by the government and not by the thousands of foreign investors who have been attracted by the quality of the Filipino workforce and competitive fiscal incentives. These incentives compensate for higher business costs for labor, logistics, power, and others.

Now, at a critical crossroads, the Senate is asked to approve a major tax and fiscal incentives bill with important benefits to the economy. The resulting law will greatly determine the volume of future inflows of reshoring manufacturing firms. Will they locate in the Philippines or continue to decide to stay away and invest elsewhere.

Exisitng investors under the 5% GIE incentive and operating ROHQs are being asked to transition to more expensive tax regimes, when their future operations are uncertain at best and severely impacted at worst.

The requested five year delay in starting the new fiscal regime for existing investors will demonstrate the support of the government for the conditions key export sectors of the economy face when their current and future operations are highly uncertain.

New investors will also observe how the government has accommodated these concerns. We all want a win-win to avoid contractions and job losses by existing investors and to attract a large share of the huge amounts of manufacturing investment relocating into Southeast Asia.

Last Paragraph of New Section 311 (C) – on Footloose Project or Activity

We recommend that the last paragraph of Section 311, particularly the 2nd requirement for the qualification of a footloose project or activity to be reworded, as follows:

> *"For purposes of this Section, a footloose project or activity shall meet all of the following conditions: (1) It is is a manufacturing activity or project;*

(2) it has a labor cost to depreciation expense of capital equipment ratio of at least 70% for three consecutive years immediately preceding the year of implementation of this Act; xxx xxx"

New Section 312 - Structural Adjustment Fund

We strongly recommend that SB 1357 adopt the Structural Adjustment Fund proposed under HB 4157 to support the IT-BPO industry to help prepare Filipino employees maintain their competitive advantage and employability. We believe that the Structural Adjustment Fund of PhP 5 Billion will be a major and critical aid in training Filipino employees to graduate from standard voice calls into higher value-added services like software development, robotic processes and automation, and even R&D for artificial intelligence.

New Section 10 (A) (6) and Section 10 (B) (1) – (removal of IPA's authority)

Finally, our strong clamor is to retain the full authority of PEZA, SBMA, CDC, and other IPAs' full authority to process and approve applications for registration of registrable projects or activities under the SIPP. We believe that credit should be given where credit is due and given their proven track record of efficiency for so many years, the trust and confidence of foreign investors in these IPAs as corruption-free agencies, and their ability to promote the Philippines and attract foreign investments into the country, the said bodies should be allowed to retain their powers and functions.

We believe that the safeguards put in place by the government such as TIMTA and all the administrative reporting requirements placed on zone registrants are more than enough check-and-balance mechanisms already to make sure that the agencies do not overstep their authority.

In this regard, we respectfully **request the deletion of new Section 10 (A)(6) and Section 10(B)(1) in SB 1357.**

In conclusion, we look forward to working with you and your Senate colleagues as you move to complete consideration of the CITIRA (CREATE) SB 1357. We are all aware that CITIRA (CREATE) was planned in better economic times. However, now it must be adjusted as a vital stimulus measure of the national government needed to strengthen investment flows when the world is facing the worst economic downturn since the Great Depression.

We trust our comments and suggestions will merit your consideration in the deliberations of this bill and look forward to any questions you may have.

Sincerely yours,

PETER HAYDEN
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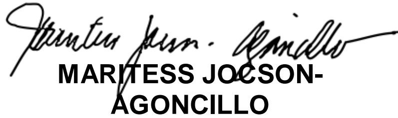
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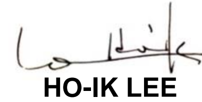
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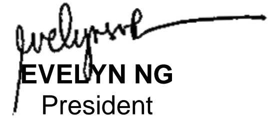
Management Association
of the Philippines


EVELYN NG
President
Philippine Association of
Multinational Companies
Regional Headquarters, Inc.

FRANCISCO ZALDARRIAGA
President
Philippine Ecozones Association

DANILO LACHICA
President
Semiconductor & Electronics
Industries in the Philippines, Inc.

MICHAEL MICHALAK
Senior Vice President and
Regional Managing Director
US-ASEAN Business Council

Attachments: 1. Matrix comparing the Philippines and Vietnam
2. Matrix comparing amendments recommended in this paper and CREATE

Copy: All senators
DOF Sec. Dominguez
DOF Asec. Lambino
DTI Sec. Lopez
DTI Usec. Rodolfo
NEDA Act. Sec. Chua
PEZA DG Plaza