October 5, 2020

BUSINESS GROUPS SUPPORT GRANDFATHERING, CONTINUITY, FOR ZONE EXPORTERS AND ROHQS IN THE CREATE BILL

Business groups are calling for Congress and the President to support proposals currently under debate in the Senate in the CREATE bill **to support export industries located at Philippine export and special zones and regional operating headquarters and to protect jobs of employees.**

Over 3,000 firms - almost all foreign-owned - engaged in manufacturing, business processing, and regional headquarters and employing nearly 2 million Filipinos are facing large increases in their future income taxes. The firms are predominantly American, Australian, Canadian, European, Korean, and Japanese. Some have operated in the country for decades, while others decided to invest in the Philippines more recently because of the quality workforce and fiscal incentives.

While located throughout the country, the firms are concentrated in Metro Manila, Baguio, Central Luzon, CALABARZON, Cebu, and Davao. Their products and services comprise the Philippines' participation in a number of regional and global supply chains.

These investors are categorized by the World Bank as "efficiency seeking" and the fiscal incentives granted to them compensate for higher logistic, power, and other costs in the Philippines. Given that such costs are lower in many other ASEAN countries attracting investment, because they subsidize electricity for manufacturing, have fewer non-working holidays, and more efficient airports and seaports, the consistency of these incentives are critical to the global investment competitiveness of the Philippines.

The proposed CREATE bill is the fourth version of a tax bill since December 2017 which, as originally drafted, would have resulted in many of these firms downsizing or departing the country. Each subsequent version of the legislation made adjustments to encourage the firms to continue to expand in the Philippines.

With the COVID-19 pandemic ongoing, UNCTAD has predicted FDI in Emerging Asia in 2019 to be -35 to -50% below 2019 and unlikely to return soon to pre-pandemic levels. Under these conditions, competition for reduced investment flows will intensify.

The pandemic has raised production costs for export firms, whose foreign markets have been badly impacted with depressed economic growth and massive employee layoffs. For this reason, the **companies proposed a five-year pause**

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before CREATE's tax reforms would apply to their operations and provided suggested language to the Senate in a letter shared with all senators.

However, as industry position papers always explained, the export **firms preferred the status quo** to continue the tax provisions they had been promised over the years to attract them to locate in the Philippines. These provisions were introduced 25 years ago after destabilizing coups, the Pinatubo eruption, and the turnover of empty military bases at Clark and Subic when the government became serious about attracting foreign investment. To attract investors, after the initial income tax holiday (ITH) incentive expired, a 5% gross income earned (GIE) tax would apply. Investors were told this rate would continue indefinitely, and they believed the government.

But today the government talks about imaginary "lost revenue," and seems unhappy that the firms have been profitable and expanded operations in the country. They are likewise insisting that companies will invest regardless of incentives. However, these firms face stiff competition with competitors in the global market and should not be similarly treated like domestic market firms. Clearly, given the closure of numerous ROHQs after TRAIN 1 took away their 15% preferential tax rate, it is undeniable that tax incentives matter. Incentives are, in many instances, one of the fundamental considerations for a company's decision to continue investing in a country.

Senate president pro tempore **senator Ralph Recto is proposing a grandfather provision to allow these export firms to continue to use their current incentives.** Sixty thousand workers are employed at these firms located at zones in the senator's hometown of Lipa, Batangas. Senator Recto wants them to keep their jobs and to attract more investment to locate on the hundreds of hectares of available land in Lipa export zones. These must also be the concerns of other government officials whose cities host export zone investors.

Senator Recto recently argued in the Senate that, after a transition period of 4, 5, 7, or 9 years, CREATE will double the income tax on most export firms located in Batangas. He is concerned these firms will leave, more firms will not invest, and Lipa will have fewer instead of more workers employed.

Senate Ways and Means Committee chairperson Pia Cayetano has done a remarkable job of managing a very complex bill. Along with her House counterpart, they have brought the bill closer to the desk of President Duterte.

She has said that these firms, when their incentives expire, can apply for new incentives so long as they continue to meet the employment, export, investment, and other conditions for which they received incentives.

In interpellation on September 29, Senator Cayetano stated: *"There can be an extension not longer than 12 years. It's actually a 4-year extension, not to* *exceed 12 years. After that, you can reapply again. There is no prohibition to reapply. It just depends on the SIPP. For so long as your business is captured by the SIPP, then you can apply and then they will evaluate you."*

But the text of SB 1357 is still not clear whether existing registered business enterprises (RBEs) can register expansion activities and/or renew incentives, if qualified, after their incentives expire. In other words, there is nothing in SB 1357 that explicitly states existing RBEs can register their expansion activities or renew 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 House Ways and Means committee chair Cong. Joey Salceda and former DOF Usec. Karl Chua in various fora and now by Senator Cayetano.

To avoid confusion, we reiterate a recommendation made in our position paper to make it clear that existing RBEs can register their expansion or renew their incentives after the transition periods provided for under CREATE.

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.

We urge that this addition for a new Section 304 (f) be included in an amendment to SB 1357. At the same time we strongly support the grandfathering proposal of Senator Recto, which will cover all IPAs and ROHQs approved under RA 8756.

We thank all the legislators and government officials who have listened to the arguments of export zone investors since 1995 when the DOF first proposed to rationalize fiscal incentives. We have always supported the goal of rationalization to achieve uniformity among IPAs to remove redundancy and unnecessary incentives. In the highly competitive world of global trade, the right menu of incentives remains necessary to retain existing investors and to attract new ones in order for the Philippines to catch up with countries such as Indonesia, Malaysia, Thailand, and Vietnam.

Approved by the following business organizations:

American Chamber of Commerce of the Philippines
Australian-New Zealand Commerce of the Philippines
Canadian Chamber of Commerce of the Philippines
Confederation of Wearable Exporters of the Philippines
European Chamber of Commerce of the Philippines
Information Technology and Business Process Association of the Philippines

PAMURI

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