Corporate Income Tax and Incentives Rationalization Act

Senate Bill No. 1357 (Package 2)

Corporate Income Tax and Incentives Rationalization Act – Package 2

In brief

On 17 February 2020, the Senate Committee on Ways and Means submitted Senate Bill (SB) No. 1357, its own version of the Corporate Income Tax and Incentives Rationalization Act or CITIRA bill.

The CITIRA bill is the second (2nd) Package of the comprehensive tax reform program (“CTRP”) of the government, which proposes to gradually lower the corporate income tax rate and rationalize corporate tax incentives to enhance fairness, improve competitiveness, plug tax leakages, and achieve fiscal sustainability.

SB No. 1357 proposes several changes from the version of the House of Representatives (House Bill No. 4157) which include, among others, new categorization for projects that would avail of the income tax holiday (ITH), 8% special corporate income tax (SCIT) based on gross income, and longer sunset period for projects that would satisfy certain conditions.

The CITIRA Bill shall still undergo both Senate and Bicameral deliberations.

The salient provisions of the CITIRA are as follows:

	House Bill No. 4517	Senate Bill No. 1357
• Corporate income tax rate for domestic corporations, resident foreign corporations (RFCs); and non-resident foreign corporations (NRFCs) shall be reduced by 1% point every year beginning 1 January 2020 until 1 January 2029, i.e. 20% beginning 1 January 2029	✔	✔
• Repeal of the 15% branch profits remittance tax (“BPRT”) exemption of Philippine branches registered with the Philippine Economic Zone Authority (“PEZA”); repeal of the 10% special income tax rate of offshore banking units (OBUs); repeal of the 10% special income tax rate of regional operating headquarters (ROHQs) within 2 years from the effectivity of the law	✔	✔
• Increase in income tax rates of: (a) interest income derived by RFCs from a depository bank under the expanded foreign currency deposit system from 7.5% to 15%; and (b) capital gains tax on sale of shares of stocks not traded in the stock exchange by RFC and NRFCs from 5%/10% to 15%	✔	✔
• 40% optional standard deduction (“OSD”) on gross income shall be applicable only to individuals (except non-resident aliens) and Micro, Small and Medium Enterprises (“MSME”) as determined by the Department of Trade and Industry	✔	
• Expansion of tax-free exchange transactions under Section 40 (C)(2) of the Tax Code	✔	
• Introduction of a general anti-avoidance rule	✔	
• Removal of the option to apply for the issuance of tax credit certificate on the refund of input VAT attributable to zero-rated sales	✔	
• Increase in penalties and imprisonment period for specific violations of the Tax Code	✔	

Rationalization of Tax Incentives

- Registered projects or activities under the Strategic Investment Priority Plan ("SIPP") shall be entitled to the following incentives:

A. Income Tax

House Bill No. 4157

- Income Tax Holiday ("ITH") shall be granted for a maximum period of 3 to 6 years. After which, in lieu of the ITH, either the preferential income tax rate of **18% (which shall be reduced to 13% by 2029) or the enhanced deductions may be applied for a maximum period of 2 to 4 years.** The incentive period varies depending on which area the registered project or activity will be located.

Area	ITH Period	Period to avail preferential tax rate or enhanced deduction
a. National Capital Region (NCR)	3 years	2 years
b. Areas adjacent to Metro Manila composed of Laguna, Bulacan, Cavite, and Rizal	4 years	3 years
c. All other areas not covered by a and b	6 years	4 years

Senate Bill No. 1357

- **The period for the availment of incentives shall follow three categories: A (Basic), B (Enhanced), and C (Advanced).**
- **The ITH may be granted for a maximum period of 4 years. Thereafter, it may avail of the Special Corporate Income Tax ("SCIT") rate of 8% in 2020, 9% in 2021, 10% in 2022 and onwards, which shall be based on gross income, in lieu of all taxes, both national and local. The SCIT period of availment may be from 3 to 4 years.**
- **In lieu of the ITH and the SCIT, enhanced deductions may be availed by the registered activity.**

Category	ITH Period	SCIT Period	Enhanced Deductions Period
a. A (Basic)	2 years	3 years	5 years
b. B (Enhanced)	3 years	4 years	7 years
c. C (Advanced)	4 years	4 years	8 years

House Bill No. 4157	Senate Bill No. 1357
• The following **enhanced deductions may be granted after the expiration of the ITH**, subject to certain conditions, and if the taxpayer would not avail of the preferential income tax rate: a. depreciation allowance for qualified capital expenditure b. 50% additional deduction on direct labor expense c. 100% additional deduction on research & development ("R&D") expenses d. 100% additional deduction on training expenses e. 100% infrastructure development f. reinvestment allowance to manufacturing industry g. enhanced net operating loss carry over ("NOLCO") h. domestic input expense used in registered export activity	• **The following enhanced deductions shall be granted subject to certain conditions:** a. depreciation allowance for qualified capital expenditure b. 50% additional deduction on direct labor expense c. 100% additional deduction on R&D expenses d. 100% additional deduction on training expenses e. 50% domestic input expense used in registered export activity **f. 50% power expense used in registered export activity** g. 50% reinvestment allowance to manufacturing industry h. enhanced NOLCO
• **Specific industries as determined by the FIRB** may be entitled to the other special deductions in lieu of the ITH or 18% preferential tax rate.	• **The Fiscal Incentives Review Board ("FIRB") and the Board of Investments ("BOI") shall prescribe the terms and conditions on the grant of enhanced deductions, including the appropriate level of percentage deductions.**
• The availment of the income tax incentives shall **not be extended beyond the initial grant (i.e. 3 to 6 years for ITH, 2 to 4 years for preferential income tax or enhanced deductions, except for (1) additional special deductions on infrastructure development and enhanced NOLCO; (2) agribusiness projects located outside Metro Manila and other urban areas; (3) projects in areas recovering from armed conflict/major disaster; and (4) projects relocating from Metro Manila and selected urbanized areas adjacent to Metro Manila to other areas of the country.**	• The availment of the **SCIT or Enhanced Deductions may be extended by three (3) or four (4) years depending on the category, subject to the qualifications under the Strategic Investment Priority Plan ("SIPP") and performance review by the FIRB. The total period for the availment of incentives shall not exceed twelve (12) years.**

B. Customs Duty Incentives

House Bill No. 4157	Senate Bill No. 1357
• 5-year maximum period to avail of exemption from customs duty on importation of capital equipment and raw materials directly and exclusively used in the registered activity (The 5-year period shall not apply to freeport zones) • 5-year maximum period to avail of exemption from customs duty on importation of capital equipment only on expansion projects	• **Duty exemption on importation of capital equipment, raw materials, spare parts or accessories that are directly and exclusively used in the registered activity. The 5-year limitation, as proposed under HB 4157, was removed.**

C. VAT Incentives

House Bill No. 4157	Senate Bill No. 1357
• VAT-exempt importation and VAT zero-rating on domestic purchases for registered enterprises located within an economic zone, freeport, or those utilizing customs bonded manufacturing warehouse, subject to the following conditions: • 90% export sales threshold is met • 90% export sales threshold is not met but complies with the rules on electronic receipts and invoices • Registered enterprises that will not meet the 90% export threshold or are located outside an economic zone or freeport (regardless of the export sale threshold) shall be subject to VAT; export registered enterprises are entitled to refund the VAT paid on importation of capital equipment and raw materials	• VAT-exempt importation and VAT zero-rating on domestic purchases for goods and services directly and exclusively used in the registered activity by registered business enterprises located in an ecozone or freeport.

Transitory Provisions for Existing Registered Activities

House Bill No. 4157	Senate Bill No. 1357
Section 310 • **<u>Those under ITH shall be allowed to continue with the availment for the remaining ITH period or for a period of 5 years, whichever comes first</u>**. • Those under the 5% GIT incentive shall be allowed to continue based on the following schedule: ○ 2 years - for registered activities under the 5% GIT regime for > 10 years ○ 3 years - for registered activities under the 5% GIT regime for 5 to 10 years ○ 5 years - for registered activities under the 5% GIT regime for < 5 years • **<u>The 5% GIT shall commence after the ITH period has lapsed only for the remaining years within the 5-year period</u>** • Existing registered activities which will qualify for registration under the SIPP may opt to be governed by the provisions of the CITIRA. In such case, the registered enterprise shall surrender its certificate of registration, which shall be deemed as an express waiver of their privilege to avail of incentives provided in the incentives law under which they were previously registered	**Section 311. Additional provisions:** • Registered business enterprises whose projects or activities were granted only an ITH prior to the effectivity of CITIRA shall be allowed to continue with the **<u>availment of the ITH for the remaining period of the ITH as specified in the terms and conditions of their registration.</u>** • **<u>Registered projects or activities which were granted ITH prior to the effectivity of CITIRA and that will expire within 5 years therefrom and entitled to the 5% GIT after the ITH, shall be allowed to avail of the 5% GIT for the remaining period after the ITH not to exceed 5 years from effectivity of CITIRA.</u>** • Those under 5% GIT shall be allowed to continue based on the following schedule: ○ 2 years - for projects or activities availing of the 5% GIT regime for > 10 years ○ 3 years - for projects or activities availing of the 5% GIT regime for 5 to 10 years ○ 5 years - for projects or activities availing of the 5% GIT regime for < 5 years ○ **<u>7 years - for projects or activities which will satisfy any of the conditions: (i) registered exporters that export one hundred percent(100%) of their goods and services; (ii) registered business enterprises 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 CITIRA; or (iii) registered enterprises engaged in footloose projects or activities.</u>** **<u>A footloose project or activity shall meet all of the following qualifications: (1) it is a manufacturing activity or project; (2) it has a direct labor expense to asset ratio of at least seventy percent (70%) for three consecutive years immediately preceding the year of implementation of CITIRA; (3) it exports one hundred percent (100%) of its manufactured goods; and (4) its actual area of operation is outside Metro Manila: *provided, that*, the FIRB may modify the direct labor expense to asset ratio or the manufacturing export requirements, upon the recommendation of the BOI, consistent with the SIPP.</u>** • Existing registered activities which will qualify for registration under the SIPP may opt to be governed by the provisions of the CITIRA. In such case, the registered enterprise shall surrender its certificate of registration, which shall be deemed as an express waiver of their privilege to avail of incentives provided in the incentives law under which they were previously registered.

Let’s talk

To help you understand and appreciate the CITIRA Bill provisions, please contact:

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Thank you

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