DoF's Diokno concedes 'new workforce models' needed for BPO industry

THE GOVERNMENT will support new modes of deploying workers as the business process outsourcing (BPO) industry transitions to a new regulator which will be more permissive of work-from-home (WFH) arrangements, Finance Secretary Benjamin E. Diokno said.

"The Philippine government stands ready to support the continued growth of IT-BPM companies by building an enabling business environment in order to boost the country's competitiveness in the field of business processes and services," Mr. Diokno was quoted as saying by the Department of Finance (DoF) in a conference last week.

The BPO industry, also known as the information technology and business process management (IT-BPM) industry, is seeking to maintain its ability to offer WFH arrangements to its employees, embroiling it in a dispute with the government.

The law requires BPOs registered with the Philippine Economic Zone Authority to perform most of their work within economic zones in order to continue enjoying their tax breaks. As a solution, the government has proposed a transfer of registration to the Board of Investments, which does not enforce the economic zone requirement.

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The Fiscal Incentives Review Board has said the transfer of registration will "resolve the sector's long-standing issue on tax incentive claims while performing business activities beyond their zone limits."

"Given the global contact center and business processing services markets' exponential growth in the past 15 years, the DoF strongly recognizes the need to integrate new, adaptive, and sustainable workforce models to boost the Philippines' competitiveness in the field of business processes and services," Mr. Diokno said.

The industry is expected to generate up to 1.1 million direct jobs by 2028.

"In the Asia-Pacific region, the Philippines remains one of the most preferred locations for delivering business processing and contact center services," according to the DoF.

"Moreover, with various firms employing new techniques and work models, the IT-BPM sector has effectively set the stage for digitalization to flourish in the Philippines," it added.

Mr. Diokno also noted that the COVID-19 pandemic was a catalyst for the industry to evolve even faster, resulting in a "dynamic, reliable, and significantly more agile IT-BPM industry that is aligned with the DoF's push for a sustainable and digitally-powered economy." — **Luisa Maria Jacinta C. Jocson**

Senate sets third week of November as target for passing budget measure

THE SENATE is confident of passing its version of the proposed P5.268-trillion budget for 2023 by the third week of November, with the conclusion of budget hearings as scheduled.

"I am grateful to all our hardworking Senators for ably steering their respective sub-committees, and for keeping us on track with our budget timeline," Senate President Juan Miguel F. Zubiri told reporters in a Viber message on Monday.

"With everyone (bringing) the same work ethic and urgency to the plenary, we expect to spend about two weeks in marathon deliberations, and we hope to be able to approve the budget as early as the third week of November," he added.

The chamber hopes to wrap up plenary debate by mid-November for passage on final reading by the following week. The rest of the year is expected to be taken up by the bicameral conference committee before the harmonized legislation is sent for the President's signature by mid-December.

"I am very glad to report that the Senate is fully on track with the budget schedule that we have laid out," Mr. Zubiri said.

"Over the course of the hearings, our sub-committees carefully combed over our agencies' programs and spending vis-à-vis the proposed P5.268-trillion budget, to ensure that the 4.9% increase from this year's budget is warranted and is crucial to the country's continued recovery from the pandemic," he added.

He said when sessions resume in November, the committee report will be sponsored promptly to immediately kick off further deliberations at plenary level.

Plenary sessions adjourned on Oct. 1 and are scheduled to resume on Nov. 7. — **Alyssa Nicole O. Tan**

Swiss see ties with PHL focused on innovation, cite red tape concerns

By Alyssa Nicole O. Tan
Reporter

THE Swiss chamber of commerce said it expects areas of cooperation with the Philippines to center on innovation, but called on the government to simplify its trade processes and benchmark against regional power and labor costs to allow investors to scale up.

"For the Swiss Chamber of Commerce of the Philippines (SwissChamPH), we are aligning the priority areas of both Switzerland and the Philippines," SwissChamPH Chairperson Christine Fajardo told *BusinessWorld* on the sidelines of the Swiss Embassy's Innovation Exhibit.

"SwissChamPH aims to position the Philippines as a stable business location for investment growth," she added. "We look forward to collaborating in areas where there are synergistic solutions."

Switzerland's priority industries, based on economic impact, are the mechanical, electrical, and metal or MEM industry; infrastructure; food; cleantech; financial technology; and medical technology, she said.

Trade Secretary Alfredo E. Pascual, speaking at the event, said the Philippine priorities are to embrace the fourth industrial revolution by harnessing new technology such as artificial intelligence and smart manufacturing.

"The strategy will involve accelerating the small business growth by enabling them to scale from small to medium and from medium to large," Mr. Pascual said.

"We will integrate our production systems for instance, by leading manufacturing, agriculture and services," he said. "We will deepen our global value chain participation, pursue aggressive trade and investment policy, and diversify our exports trade and investment partners."

Other areas of focus include developing human capital and building capacity, supporting regional industrial transformation, and making the economy more attractive to investment.

Some of these priorities, Ms. Fajardo said, are aligned with Swiss areas of focus. "This is clearly aligned, in terms of what we can prioritize and it's a wide spectrum, so there's a lot of opportunity areas," she said.

She said SwissChamPH has sought to develop innovation initiatives in three areas — health and life sciences, manufacturing, and retail.

One of the immediate goals of this initiative is "a white paper on priority areas and let's say the challenges and opportunities, and then recommend priority projects for the companies in terms of collaboration," Ms. Fajardo said.

The chamber, she added, has done the most advanced work in the health and life sciences cluster, noting that it is prepared to expand its membership to more Swiss and Filipino businesses in various industries.

The targets for membership expansion are those businesses seeking to initiate and maintain links with Switzerland, gain a foothold in both the Philippine and Swiss markets, and participate in the broader markets of the Association of Southeast Asian Nations and Europe.

Swiss Ambassador to the Philippines Alain Gaschen told the media during the event that: "We have a whole page of potentials, so pharmaceutical is one... We also see a lot of potential in the cleantech industry and infrastructure."

He also mentioned railways as a possible area of collaboration.

"We looked into processed food, natural ingredients and textiles, and these have huge potential," he said.

The requirements of the Swiss market in the event of collaboration are that "You have to deliver on time, package it properly, label it properly, and you have to have the quantities and the quality that is required for the European market, but we have a guide for those industries step by step that we can share, and then we open for business," he added. "So basically, there's a lot that can be done."

He said the Philippines presents obstacles in scaling up such businesses.

"Electricity (is) a challenge to infrastructure," Mr. Gaschen said, adding that red tape and market access are also deterrents to investment.

The general manager of biotech company Roche, Diana Edralin, said, "One of the things that we can really (focus on) in terms of something concrete in healthcare, is predictability in the review and approval of innovative medicines and devices."

"I know that the Philippine FDA (Food and Drug Administration) has now made bold steps in approving the reliance pathway," she added, referring to an international best practice in which a national regulator takes into account approvals granted by other national regulators in evaluating products such as pharmaceuticals for its own market.

Ms. Edralin said she recognizes the FDA's eagerness to fully implement the reliance pathway to speed up the approval process.

She noted that prior to the pandemic, it took about two to three years for the Philippines to approve a lifesaving innovation, device, or diagnostic procedure.

"During the pandemic, we were able to see that we can actually find agile and flexible ways on how to go about ensuring that we simplify the processes to allow for innovation to happen," she said.

"The second opportunity in healthcare is again how we are fully funding and implementing Universal Health Care, and the National Integrated Cancer Control Act, even the Rare Conditions Act, properly," she said.

"So, these are really wonderful laws, but if you want further innovation to happen, I think there's an opportunity for us to make sure that the provisions within those laws, again, allow for innovation and exchange through public-private partnerships," she added.

Construction and Industrial company Sika Philippines, Inc. General Manager Christophe Lejeune said that the cost of power and labor in the Philippines is uncompetitive.

"I think it's important for the DTI (Department of Trade and Industry) and for other government agencies to look around what's happening in Asia Pacific, so that they can benchmark and look at ways to contribute to making the country more efficient," he said.

"The Philippines is a very attractive market. As the ambassador was mentioning, you're talking about 110 million people in the housing sector and construction sector," he added, "so some things could be improved so that we can work faster and better."

Holcim Philippines, Inc. Chief Executive Officer Horia Adrian said, "the word that is important here is efficiency."

"There are higher costs for labor, for electricity, but at the end of the day, there are solutions to bring these costs down, and these solutions are built with innovation," he said.

"I think it is important to accelerate this reduction of bureaucracy in terms of permitting," he added. "If you have a faster way to build innovation, to build efficiency, then this has to be facilitated. And that's for me the important message here, to create a level playing field with other countries abroad and to make sure that we as a country are accelerating the growth because there will be a need for growth in the Philippines."

OPINION

What's #TRENDING? Understanding and documenting industry analysis

LET'S TALK TAX
CHRISTIAN DERICK D. VILLAFRANCA

In our last article on the fundamentals of entity characterization in transfer pricing documentation (TPD), we highlighted the concept that our knowledge of the nature of a particular business determines the entity characterization and in turn, the entity characterization influences the direction and tone of the TPD as well as setting the direction in having a meaningful comparison of the price or level of income of the entity in a controlled transaction against the price or level of return from similar independent transactions.

Now, let's talk about Industry Analysis (IA) and how it affects the preparation of TPD as discussed in Revenue Regulations (RR) No. 2-2013 or the Transfer Pricing Guidelines and Revenue Audit Memorandum Order (RAMO) No. 1-2019.

WHAT IS INDUSTRY ANALYSIS?

The Transfer Pricing Guidelines provide that the details of the TPD should include the nature of the taxpayer's business, and the industry and market conditions where it operates.

IA provides an understanding of the relevant economic circumstances or market conditions in which the taxpayer's business operates in determining market comparability in order to make meaningful comparisons of prices or margins.

Analysis of the taxpayer's industry shall be done with consideration to several factors, including main characteristics of the taxpayer's business and performance of the industry. By understanding the taxpayer's industry, the expected level of price or return by the taxpayer can be known.

The profitability of an industry is influenced, among others, by any or a combination of the following forces:

1. Macroeconomics (e.g., interest rates, inflation, rate of economic growth, etc.);
2. Demographic (i.e., the qualities, such as age, sex, and income, of a specific group of people);
3. Governmental factors (e.g., political climate, tax incentives available, war and conflicts, etc.);
4. Geographical location; and
5. Technological advancements.

In economics, similar firms operating in the same industry would generally tend to yield similar returns over time. In layman's terms, if Company A sells the same product as Company B, both companies should generally yield a similar level of profitability, *ceteris paribus*. Anchored in this concept is the transfer pricing procedure where the related party transaction will be benchmarked or compared against independent comparable companies belonging to the same industry.

For instance, Company A is rendering shared services to its related parties. Company A will be benchmarked against other companies in the business process outsourcing (BPO) industry. Companies under this industry are usually characterized as routine support service providers and normally apply a pricing model of costs plus mark-up. As a routine support service provider, there is an expectation that the level of profitability of Company A will generate and maintain a consistent level of profitability when compared with that of the other companies in the BPO industry.

The BPO industry in the Philippines, in general, can be considered a profitable sector and companies belonging to this industry are doing well financially. Now, if Company A reports a net loss or low returns, this may be an indication that it is not being compensated fairly. In this case, Company A needs to establish that the losses or low level of profitability are commercial in nature within the context of its characterization and industry performance and not because of the special relationship with the related party.

How does IA affect the comparability of prices and level of return?

Prices may vary across different markets even for transactions involving the same property or services. In order to make meaningful comparisons of prices or margins between entities/transactions, the markets and economic conditions in which the entities operate or where the transactions are undertaken should be comparable.

The economic circumstances that may be relevant in determining market comparability include the availability of substitute goods or services, geographic location, market size, the extent of competition in the markets, consumer purchasing power, the level of the market at which the enterprises operate (i.e., wholesale or retail), etc.

For example, lease rates in urban areas are usually higher than in rural areas due to the high demand for housing in the developed areas because of the convenience of living in the city, where land is scarce. Also, prices of commodities are more expensive in cities because of the additional costs incurred (e.g., transportation cost, storage, etc.) in bringing these goods to the city in good condition.

Another example is the pricing offered by manufacturers to wholesalers and retailers. The prices offered to the former are usually lower than that offered to the latter. This is because of the discount granted to wholesalers who procure a larger volume of products than retailers.

In addition, government policies and regulations may have an impact on prices and margins. For example, early this year, the government imposed a ceiling on the price of selected medicines and drugs under the Maximum Drug Retail Price (MDRP) system. MDRP is the highest amount a retailer may charge to a consumer for medicine placed under price regulation. Other examples are the price cap imposed by the government on COVID-19 Rapid Antigen Test and on pork and chicken. Hence, the effects of these government regulations should form part of the discussion in TPD as part of the examination for comparability of the market and economic conditions.

SOURCES OF IA

One can refer to external sources of information, such as industry research reports, publicly available annual financial statements of the main players in the industry, data from the Securities and Exchange Commission, and other information available through the internet or in databases can be used to gain understanding of industry trends.

TAKEAWAY

There is a saying that "birds of the same feather flock together." Seeing birds flying together is very common sight. They move, flock, and feed together. You will not see an owl flying with a flock of pigeons.

In relation to transfer pricing, knowing the behavior of the industry group where your business belongs and maintaining a comparable level of profitability with other companies belonging to the same "flock" will help your company gauge if the transfer prices with related parties follow the transfer pricing guidelines.

Stay tuned for next month's article as we continue to take you through the other components of transfer pricing documentation.

Let's Talk Tax is a weekly newspaper column of P&A Grant Thornton that aims to keep the public informed of various developments in taxation. This article is not intended to be a substitute for competent professional advice.

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