Relief for banks funding Maharlika still under study, central bank says

By Keisha B. Ta-asan
Reporter

THE Bangko Sentral ng Pilipinas (BSP) said it has yet to determine whether it will extend regulatory relief to state-owned banks designated as funders of the proposed Maharlika Investment Fund.

Deputy Governor Chuchi G. Fonacier, head of the central bank's Financial Supervision Sector, said the Monetary Board will decide on possible regulatory relief measures for Development Bank of the Philippines (DBP) and Land Bank of the Philippines (LANDBANK).

"Given the scenario, the Monetary Board will relate and look at the banks' financial condition first. That's how the BSP assesses the basis to grant regulatory relief," Ms. Fonacier said.

"We don't want to grant the relief measures right away. The Monetary Board should determine whether the regulatory relief can be extended. We do not grant the relief at the onset," she said.

She added that even though DBP and LANDBANK are government banks, the BSP will still have to consider the implications on the banking system if the state-owned banks are to supply seed money to Maharlika.

Senate Bill No. 1670 proposes that the two banks provide Maharlika initial capital of P75 billion.

According to Ms. Fonacier, the government banks are in talks with the BSP on possible exemptions from the BSP's ceilings on equity investments.

"If they have equity investments, they will be subject to a ceiling. So, they are looking to be exempted from those limits and ceilings," she said.

"But again, (only) the Monetary Board has the authority to grant them regulatory relief measures. Not us (in the Financial Supervision Sector)," she added.

According to the BSP's Manual of Regulations for Banks, the equity investment of a bank in a single financial allied undertaking is capped at a certain ratio relative to the bank's total subscribed capital stock and the total voting stock of the allied undertaking.

In January, BSP Governor Felipe M. Medalla, who also heads the Monetary Board, expressed his support for the objectives of the Maharlika legislation.

"We support the provisions that say that (the central bank) may extend regulatory relief to the DBP and LANDBANK," Mr. Medalla said.

"Some critics may say that it gives undue advantage to LANDBANK and the DBP, relative to private banks, but one must be aware, too, that LANDBANK and DBP are also quite restricted by their mandates (as government financial institutions) and do not really directly compete very much with the private banks. So, we do not see that as (posing) a major competition problem," he added.

The BSP has also been proposed as a Maharlika funder at some point in the legislative process. The plans involve the central bank remitting all of its dividends to Maharlika in the first and second fiscal years after the fund's establishment.

In succeeding years, the proposals involve the BSP providing half of its dividends to the fund.

Palace announces biofertilizer program to cut import reliance

PRESIDENT Ferdinand R. Marcos, Jr. will seek to promote the greater use of biofertilizer to reduce dependence on imported petroleum-based fertilizer, the Palace said in a statement.

"We are going to introduce biofertilizer to our farmers and teach them how to use it," Mr. Marcos was quoted as saying by the Presidential Communications Office (PCO) after he met with officials from the Department of Agriculture (DA), which the President concurrently heads.

"I hope this will ease our concerns when it comes to the supply of fertilizer," he said. "And we can fully control the availability of biofertilizer."

Mr. Marcos said the shift will not immediately mean farmers would stop using non-organic fertilizers such as urea.

"There will still be a mix," he said. "But we will reduce our dependence on imports."

The DA has conducted biofertilizer trials and concluded that can it be produced domestically, according to the PCO.

"According to the chief executive, there were promising results from early tests although biofertilizer use entails some cost, but it could be brought down especially if it is going to be produced locally," it said.

During his state visit to China in January, Mr. Marcos signed deals with Chinese producers to sell fertilizer at favorable prices, the Palace said.

It said two Chinese fertilizer manufacturing companies signed a cooperation agreement with the Philippine International Trading Corp., "which could ensure a sustainable supply of much-needed fertilizer at reasonable prices." — **Kyle Aristophere T. Atienza**

Marcos rules out special powers for agri dep't to address inflation

PRESIDENT Ferdinand R. Marcos, Jr. said on Wednesday that he sees no need to take on special powers to address inflation, adding that the government is undertaking measures to mitigate its impact.

He was responding to proposals from some legislators to give the Department of Agriculture (DA), which the President heads concurrently, additional powers to help stabilize rising costs.

"I do not think that it is necessary to ask for special powers. I already have the power to declare an emergency and to control the prices of commodities," he told reporters on the sidelines of a DA event in Manila.

The government is counting on more farm-to-consumer direct-sale stores to cut out the middleman and bring down food prices.

Mr. Marcos said the government is also addressing gaps in the food supply to keep food costs under control.

Inflation hit a fresh 14-year high of 8.7% in January, accelerating from 8.1% in December as food prices remained high due to supply issues.

Inflation may rise to as much as 9.3% in February, the Bangko Sentral ng Pilipinas has said, citing the higher cost of liquefied petroleum gas, pork, fish, eggs, and sugar.

"We can't do anything about fuel. We can't do anything about other inputs," Mr. Marcos said. "But in the agriculture industry, if you disaggregate the inflation figures, it was 28% in the past. Now, it's just 11%, so that's a big deal."

Last month, National Economic and Development Authority Secretary Arsenio M. Balisacan said inflation may start to plateau in March with food supply pressures easing with the start of harvest season and the absence of typhoons so far this year.

Albay Rep. Jose Ma. Clemente S. Salceda said last year that Mr. Marcos should be given powers to incentivize production and provide loans and guarantees to agricultural suppliers.

The special powers he proposed included anti-price-gouging rules to deter the sale of essential goods at "excessive" prices and the power to initiate investigations into possible abuses in pricing energy and essential goods. — **Kyle Aristophere T. Atienza**

Miners welcome foreign investment unlocked by RCEP

By Sheldeen Joy Talavera

MINERS said they welcome any foreign investment that may be encouraged by the Regional Comprehensive Economic Partnership (RCEP) trade deal.

"Any opportunity that would encourage and attract investment to the mining industry is most welcome," Rocky G. Dimaculangan, vice-president for Communications of the Chamber of Mines of the Philippines, told *BusinessWorld* in a Viber message.

He added that such investment will help develop capital-intensive metals mining projects.

"We can also benefit from any technological improvements and best mining practices that foreign investment can bring," he said.

The association also looks forward to the "liberalization of trade services," which will broaden the market for mining professionals and suppliers.

Dante R. Bravo, president and chief operating officer of Global Ferronickel Holdings, Inc., said that the agreement has the potential to expand trade significantly among participating countries.

"The entry of more foreign mining companies in the Philippines will be good as this would accelerate the exploration and development of our mining potential, enhance sharing of best practices, and develop or facilitate transfer of technology to optimize use of our resources," he said in a text message.

Francis Joseph G. Ballesteros, head of Public and Regulatory Affairs of Philex Mining Corp., said: "I don't think the RCEP will have a direct impact on the mining industry, but any effort to expand global market access and opportunities for Philippine exports, even to increase investments in the country, should be welcome."

Jose Bayani D. Baylon, senior vice-president and chief sustainability officer of Nickel Asia Corp., downplayed the trade deal's impact because mining is not an "open market" because companies are locked into long-term contracts with their customers.

"Foreign mining interests have been coming and going and some stay and some don't. (I am) not so sure the RCEP will change that," he said.

FTAs crucial as Philippines approaches upper middle-income status

THE Philippines' progress to upper middle-income status will make concessional trade privileges harder to come by, making free trade agreements (FTAs) with blocs like the European Union (EU) a matter of urgency in order to lock in advantageous trading terms, the Department of Trade and Industry said.

Trade Secretary Alfredo E. Pascual told reporters on the sidelines of the Mega Global Corp.'s cannery inauguration in Sto. Tomas, Batangas on Wednesday that the Philippines will be ineligible for the EU's Generalized Scheme of Preferences Plus (GSP+) trading scheme once it becomes an upper middle-income country.

"As an upper middle-income country, the Philippines will no longer be eligible for GSP+," Mr. Pascual said.

As such, Mr. Pascual highlighted the importance of "resuming our discussions on a full-fledged FTA between the Philippines and EU."

On Feb. 22, Mr. Pascual met with members of the EU Parliament subcommittee on human rights to discuss the GSP+ renewal, a possible FTA, and improving economic relations.

The last round of FTA negotiations between the Philippines and EU was in 2017.

The GSP+ is available to low and lower middle-income countries. To maintain eligibility, countries are required to implement 27 international conventions related to human and labor rights.

Philippine eligibility for GSP+ is set to expire at the end of 2023.

In December, the National Economic and Development Authority said that the Philippines is projected to hit upper middle-income status in 2024 or 2025.

According to Mr. Pascual, the EU delegation was receptive to proposals to resume negotiations.

"With or without the requirements of EU, we are observing the principles that they are interested in," Mr. Pascual said.

"Our own agencies are very much aware of the principles and we are a signatory to a number of international conventions," he added. — **Revin Mikhael D. Ochave**

OPINION

PDRs as an instrument for capital raising

TAXWISE OR OTHERWISE
SYLVIA B. SALVADOR

Raising capital and expanding foreign investments are pivotal in furthering Philippine economic development. It is crucial, however, to align these important factors with the rights of Philippine citizens to engage in certain activities expressly reserved to them under the Philippine Constitution such as public utilities, mass media and land ownership. To cite a few undertakings, the foreign equity ceiling for the operation of public utilities and companies owning land is 40%; while ownership and management of mass media is reserved solely for Philippine citizens.

As a government initiative to open the Philippine economy, Republic Act (RA) No. 11659 was passed on March 21 amending the Public Service Act of 1935. It liberalized the foreign equity limitations on public utilities imposed by the Constitution by defining "public utility" for the purpose of applying foreign equity limitations. RA 11659 narrowed the list of public utilities to any public service that operates, manages, or controls for public use the distribution of electricity and water, and public utility vehicles, among others. Thus, foreign companies may now wholly manage, operate and control telecommunications, shipping and railways.

Parallel to this government action of expanding the avenue for foreign investments is the raising of capital by businesses. This may be done by issuing debt and securities.

One such security is Philippine Depository Receipts (PDRs). In certain instances, the parent holding company (HoldCo) issues PDRs to investors to source funds for its operating subsidiary (OPCo) which is engaged in wholly or partially nationalized activities.

Considering that a PDR is not a simple form of investment unlike shares of stock, it is crucial to understand the complexity of its tax implications, e.g., the tax impact of issuing PDRs and of dividends received by a foreign PDR holder.

The Court of Tax Appeals (CTA) recently issued a decision with a comprehensive analysis of the nature of PDRs and related tax implications of the involved transactions (CTA Crim. Case Nos. O-679 to O-682 dated Jan. 18, 2023). The HoldCo issued PDRs to its investor to raise capital for its OpCo. The Bureau of Internal Revenue (BIR) considered the transaction a sale of the underlying shares of stock (i.e., shares of stock of the OpCo). It imputed a gain based on the difference between the consideration for the PDRs and the cost of OpCo's shares.

There are two substantive tax issues lengthily discussed by the CTA. The first is whether the issuance of the PDRs by HoldCo is considered a sale of the underlying shares, such that any trading gain realized from the sale is taxable. The second is whether HoldCo, as the issuer of the PDRs, is a dealer in securities subject to income tax on the imputed trading gain and 12% VAT.

NO TRADING GAIN ON ISSUANCE OF PDRs

The CTA focused on the nature of PDRs to determine whether the issuance is a taxable event. It recognized that although neither the Tax Code nor the Securities Regulation Code (SRC) define the term PDR, it is classified as a security which grants the holder the right to the delivery of the sale of the underlying shares. PDRs are not statements nor are they certificates of ownership of a corporation. Further, it took cognizance of the SEC clarification that a PDR is an equity derivative since its value is dependent on the underlying equity. In the same vein, the CTA cited Philippine Stock Exchange Circular for Brokers No. 2375-99 which provides that as long as the PDRs remain unexercised by the holder, the latter has no right of ownership over the underlying shares and all such ownership rights pertain to and belong to the issuer. Upon exercise of the option, the PDR holder becomes a shareholder to the extent that such holder is qualified to own the underlying shares.

With this, the Court ruled that PDRs may fall under the classification of securities similar to shares of stock but in a different category under the SRC (i.e., derivatives like options and warrants, and other instruments as may in the future be determined by the Commissioner).

Further, the Court pointed out that there is no wording in the instruments and subscription agreements that would allow the PDR holder to become outright shareholders of the OpCo upon the issuance of the PDRs. They only retain options to purchase the underlying shares subject to certain conditions (e.g., there is no law restricting foreign ownership in the underlying shares of the operating entity).

Furthermore, the Court found that the process whereby the PDRs were issued were investment transactions and did not involve the sale of shares of stock.

Thus, the Court concluded that there is no basis for the alleged imputed trading gain upon the issuance of PDRs.

ISSUER OF PDRs NOT A DEALER IN SECURITIES

The CTA explained that a dealer is regularly engaged in the purchase and resale of securities to customers.

By comparison, HoldCo was not habitually or regularly engaged in the purchase or resale of securities. The issuance of PDRs by HoldCo is to raise capital pursuant to its authorized activities. The Court noted the SEC's acknowledgement that holding companies may engage in investment activities for their subsidiaries as indicated in their Articles of Incorporation with a limitation that said companies will not act as dealers in securities. Thus, the CTA found HoldCo not liable for VAT since it is not a dealer in securities.

DIVIDENDS FROM PDRs

Another significant tax consideration of PDRs held by a non-resident foreign corporation (NRFC) is availing of a lower withholding tax on dividends.

The BIR, for its part, recognizes the impact of PDRs in applying the tax sparing rule under Section 28(B)(5)(b) of the Tax Code. Generally, dividends received by an NRFC from a domestic corporation are subject to 25% final withholding tax. However, under the tax sparing rule, the dividends remitted are subject to a preferential rate of 15% if the country where the NRFC is domiciled allows a credit against its taxes due on the dividends, the amount of taxes deemed to have been paid in the Philippines equivalent to 10%, i.e., the difference between the 25% regular corporate income tax rate and the 15% reduced dividend withholding tax rate. Jurisprudence has also established that the lower rate of 15% also applies if the dividends are not taxed in the foreign country where the NRFC resides.

The BIR recognized that a PDR holder is typically entitled to the dividends accruing to the underlying shares. Following Revenue Memorandum Order (RMO) No. 46-2020, a PDR holder is also entitled to avail of the tax sparing rule if: (a) the PDR is coupled with a right to purchase the underlying shares; and (b) such right can be legally exercised.

The basis of the BIR's argument is that a PDR is considered a share of stock since it falls under the definition of shares of stock in the Tax Code (i.e., shares of stock include warrants and/or options to purchase shares of stock). Thus, a PDR holder is also a shareholder for purposes of this tax sparing rule.

In a post-pandemic era where the economy is almost in full swing to recovery, it is vital for both the business sector and government to work hand-in-hand to ensure continuity of the country's economic growth. With these alignment and transparency, any complexity can be fully comprehended for the smooth implementation of commercial transactions.

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