REPUBLIC OF THE PHILIPPINES
DEPARTMENT OF FINANCE
BUREAU OF INTERNAL REVENUE
Quezon City

57(B); 107(A); RR 2-98; RMC 8-2017		

Person to Contact: Chief, Law Division
Tel. Nos. 926-55-36/927-09-63

OT-471-2021
Date DEC 2 1 2021

MARUBENI-DMCI CONSORTIUM
8th Floor, LV Locsin Building, Ayala Center
Makati Avenue, Makati City

Attention: **Mr. Tomoyuki Kakiuchi**
Project Director (Contractor's Representative)

Gentlemen:

This refers to your letter dated December 13, 2019 requesting, on behalf of Marubeni-DMCI Consortium, for confirmation of your opinion, as follows:

1. The unincorporated consortium, Marubeni-DMCI Consortium (hereinafter "UC"), having been formed solely for the purpose of bidding and implementing the LRT Line 2 – East (Masinag) Extension Project under the Contract for Procurement of Trackwork, Electrical and Mechanical (E&M) Systems and Integration with Existing Systems for LRT Line 2 – East (Masinag) Extension Project with the Department of Transportation (DOTr), is not subject to the corporate income tax pursuant to the Exchange of Notes between the Government of Japan and the Government of the Republic of the Philippines;

2. Since the UC is not subject to the corporate income tax, the gross payments made by DOTr to the UC are not subject to the 2% creditable withholding tax (CWT) under Section 57 (B) of the Tax Code, as amended, and implemented by Revenue Regulations No. 2-98, as amended by Revenue Regulations No. 11-2018;

3. Being not subject to the corporate income tax, the UC is not required to file quarterly and annual income tax returns with the Bureau of Internal Revenue (BIR);

4. With respect to the onshore portion of the JICA-funded Project, pursuant to the holding of the Supreme Court in *Mitsubishi Corporation – Manila Branch vs. Commissioner of Internal Revenue (G.R. No. 175772 dated June 5, 2017)* and *Revenue Memorandum Circular (RMC) No. 8-2017*:

    a. The VAT-registered suppliers and sub-contractors of the UC shall bill and pass on the twelve percent (12%) VAT to the UC. In turn, the UC shall include in its billing and pass on the twelve percent (12%) VAT to the DOTr. Since under the Exchange of Notes, the DOTr shall assume the payment of taxes, then the VAT is for the account of DOTr;

    b. The Japanese contractors, shall file the prescribed VAT returns on gross receipts derived from the JICA-funded Project, claim its input taxes from its purchases of goods, properties, and services and shall pay the output tax thereon, after offsetting the creditable or allowable input taxes, considering that the amount intended for the payment of the VAT has already been collected and received by UC from the DOTr as part of its billing;

5. As the importer of record, the DOTr shall be liable for the 12% VAT on the importation of materials and equipment under Section 107(A) of the Tax Code, as amended;

6. The Japanese personnel employed by the UC and its Japanese contractors performing work in the Philippines pursuant to the JICA-funded Project are required to file income tax returns but the DOTr shall assume the payment of the taxes due thereunder. Accordingly, the said Japanese personnel are not subject to withholding tax on compensation under Section 57 of the Tax Code, as amended, pursuant to the tax assumption provisions under the Exchange of Notes and the holding of the Supreme Court in *Mitsubishi Corporation – Manila Branch vs. Commissioner of Internal Revenue (G.R. No. 175772 dated June 5, 2017).*

7. In connection with the tax assumption scheme and pursuant to the Exchange of Notes, the Government of the Republic of the Philippines or its executing agency (*i.e.*, DOTr) shall be responsible for the liquidation or settlement of such fiscal levies, duties, taxes, and other similar charges.

It is represented that Marubeni Corporation is a non-resident foreign corporation organized and existing under the laws of Japan with principal address at Tokyo Nihombashi Tower, 7-1, Nihonbashi 2-chome, Chuo-ko, Tokyo, Japan 103-6060. It is a Japanese trading firm engaged in various and diverse business including importing and exporting and various business activities related to infrastructure and construction. Marubeni Corporation is licensed to do business in the Philippines. Its Manila Branch (hereinafter, 'MC Manila Branch') was registered with the Securities and Exchange Commission (SEC) on March 20, 1967 to engage in the importation, exportation and sale of foreign and indigenous products, instruments, alcohol, industrial chemicals, medicines, poisonous and caustic matters, manufacture and sale of general merchandise, factor business, laying-out management and undertaking of construction works and any and all related and incidental businesses.

On the other hand, D.M. Consunji, Inc. (DMCI) is a corporation duly organized and existing under and by virtue of the laws of the Republic of the Philippines with principal address at DMCI Plaza Bldg. 2281, Chino Roces Avenue Extension, 1231 Makati City. It was registered with the SEC on December 24, 1954. It was established to engage in and carry on the trade and business of engineers, general builders and contractors; to enter into contracts in relation to, and to design, erect, build, construct, maintain, alter, repair, pull down and restore, either alone or jointly with any other companies or persons, works and construction jobs of all description including roads, bridges, warehouses, factories, engines, machinery, electric and mechanical works, drainage, and sewage, houses and buildings of every description, barracks, piers, and other edifications needed and necessary in the ordinary course of business and life; to produce, manufacture, buy, hold, sell or otherwise acquire and dispose of and deal in, lease, hire and let on lease or hire all kinds of tools, implements, supplies, equipment, machine engines, and all other materials, apparatuses, and contrivances as are necessary for the purpose or object aforesaid.

It is further represented that pursuant to an Exchange of Notes entered into between the Republic of the Philippines and the Government of Japan on March 25, 2013, for the "*Mass Transit Systems in Metro Manila (Y43.25 billion or P18.56 billion) and the New Bohol Airport Construction and Sustainable Environment Protection Project (Y10.78 billion or P4.63 billion),*" the Government of the Philippines and the Japan International Cooperation Agency ("JICA"), entered into Loan Agreement PH-P255 on March 27, 2013.

Under Section 7 of the Exchange of Notes:

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"(1) The Government of the Republic of the Philippines shall, by itself or through its executing agency, assume:

(a) all fiscal levies and taxes imposed in the Republic of the Philippines on JICA on and/or in connection with the Loan as well as interest accruing therefrom;

(b) all duties and related fiscal charges imposed in the Republic of the Philippines on the Japanese companies operating as suppliers, contractors and/or consultants with respect to the import and re-export of their own materials and equipment needed for the implementation of the Project;

(c) all fiscal levies and taxes imposed in the Republic of the Philippines on the Japanese companies operating as suppliers, contractors and/or consultants with respect to the payment carried out for and the income accruing from the supply of the products and/or services required for the implementation of the Projects; and

(d) all fiscal levies and taxes imposed in the Republic of the Philippines on the Japanese employees engaged in the implementation of the Projects with respect to their personal income derived from Japanese companies operating as suppliers, contractors and/or consultants for the implementation of the Projects.

(2) In connection with such tax assumption, the Government of the Republic of the Philippines or its executing agency shall be responsible for the liquidation or settlement of such fiscal levies, duties, taxes and other similar charges."

It is likewise represented that on August 11, 2017, Marubeni Corporation and DMCI (collectively, the UC) entered into a Consortium Agreement for the limited purpose of submitting a Tender to the DOTr and to perform the contract to be made and entered into with the DOTr, if successfully awarded to the Consortium. On August 14, 2017, the UC tendered its bid for the Project in compliance with the above Invitation for Bids.

Consequently, on December 14, 2018, DOTr Secretary, Mr. Arthur P. Tugade issued its Letter of Acceptance to the UC indicating that the UC's final offer for the execution of Procurement of Trackwork, Electrical and Mechanical Systems and Integration with Existing Systems for LRT Line 2 – East (Masinag) Extension Project and for the Accepted Contract Amount (inclusive of provisional sums, but excludes VAT, import duties, and taxes) of

Thousand Japanese Yen (JPY

US Dollars (USD) and

Euros (EUR was

accepted by the DOTr.

It is further represented that on February 6, 2019, the DOTr and the UC entered into a Contract Agreement, whereby for the performance of the Works (Procurement of Trackwork, Electrical and Mechanical Systems and Integration with Existing Systems for LRT Line 2 – East

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(Masinag) Extension Project for Capacity Enhancement of Mass Transit Systems in Metro Manila), DOTr shall pay the UC the Total Contract Amount comprised of:

> *"(a) Accepted Contract Amount of ... Philippine Pesos (Php ... /100), ... Two Thousand Japanese Yen (JPY ...), ... Thousand Six Hundred Forty-Three US Dollars (USD ...) and ... Thousand Euros (EUR ...) and (b) VAT and custom duties/taxes as estimated to be in the amount of ... Thirty- ... and 99/100 Philippine Pesos (Php ...)."*

It is represented, further, that deemed to form and be read and construed as part of the Contract Agreement are the General and Particular Conditions of Contract, which forms part of the Bid Documents. The said conditions provide:

> *"14.1 Contract Price*
>
> *Unless otherwise stated in the Particular Conditions:*
>
> *(a) the Contract Price shall be the lump sum Accepted Contract Amount and be subject to adjustments in accordance with the Contract;*
>
> *(b) <u>the Contractor shall pay all taxes, duties and fees required to be paid by him under the Contract, and the Contract price shall not be adjusted for any of these costs,</u> except as stated in Sub-Clause 13.7 [Adjustments for Changes in Legislation]*
>
> *xxx xxx xxx*
>
> *<u>Particular Conditions of Contract (PCC) – B Clause 14.1 (d)(1)(b)</u>*
>
> *(1) Notwithstanding the provision of Sub-Clause 14.1 subparagraph (b), the Government of the Republic of the Philippines shall, by itself or through its executing agency, assume:*
>
> *(a) all duties and related fiscal charges imposed in the Republic of the Philippines on the Japanese companies operating as suppliers and contractors with respect to the import and re-export of their own materials and equipment needed for the implementation of the Project; and*
>
> *(b) all fiscal levies and taxes imposed in the Republic of the Philippines on the Japanese companies operating as suppliers and contractors with respect to the payment carried out for and the income accruing from the supply of the products and/or services required for the implementation of the Project; and*
>
> *(c) all fiscal levies and taxes imposed in the Republic of the Philippines on the Japanese employees engaged in the implementation of the Project with respect to their personal income derived from Japanese companies operating as suppliers and contactors for the implementation of the Project.*
>
> *(2) In connection with such tax assumption, the Government of the Republic of the Philippines or its executing agency shall be responsible for the liquidation or settlement of such fiscal levies, duties, taxes and other similar charges."*

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Pursuant to the treaty obligations of the Philippines under the Exchange of Notes and JICA Loan No. PH-P255, the loan shall be limited to financing expenditures for goods and services from eligible source countries, *i.e.*, the UC. As the winning bidder, the UC is a bidder of an eligible source country according to the Guidelines and the Bidding Documents pursuant to the Exchanges of Notes executed on March 25, 2013. The same requirement was reiterated in Part I, Section V of the Bidding Documents ("Eligible Source Countries of Japanese ODA Loans").[1]

Under Part I, Section V, Eligible Source Countries of Japanese ODA Loans of the Bidding Procedures for the Project, the eligible nationalities of the suppliers of the Project are as follows:

> *"1. The eligible Nationality of the Supplier(s) shall be the following:*
>
> *(a) Japan in the case of the prime contractor; and*
> *(b) All countries and areas in the case of the sub-contractor(s).*
>
> *2. With regard to sub-section 1 above, in case where the prime contractor is a joint venture, such joint venture will be eligible provided that the nationality of the lead partner is Japan, that the nationality of the other partners is Japan and/or the Republic of the Philippines and that the total share of work of Japanese partners in the joint venture is more than fifty percent (50%) of the contract amount."*

Furthermore, Articles 5 and 8 of the Consortium Agreement between Marubeni Corporation and DMCI dated August 11, 2017 provides that Marubeni Corporation as the Lead Partner:

> *Article 5*
>
> *Leader and Representative of the Consortium*
>
> *1. Marubeni shall be the Consortium leader (hereinafter called the "Consortium Leader") which shall represent the Consortium in all matters relating to the Tender and shall sign all documents on behalf of the Consortium including the Tender and the Contract, if the Contract is awarded to the Consortium.*
>
> *xxx xxx xxx*
>
> *Article 8*
>
> *Scope of Work*
>
> *In general, Marubeni as a Consortium Leader will execute majority of the works, including design, engineering, integration and procurement of materials for the Project from outside of the Philippines and DMCI will execute on-shore work, including customs clearance, inland transportation, construction and installation. xxx xxx xxx"*

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[1] DEPARTMENT OF TRANSPORTATION, Capacity Enhancement of the Mass Transit Systems in Metro Manila Project - Procurement of Trackwork, Electrical, and Mechanical (E&M) System and Integration with Existing Systems for LRT Line 2 - East (Masinag) Extension Project, April 12, 2017, *available at: <http://dotr.gov.ph/2014-09-02-05-02-13/item/582-capacity-enhancement-of-the-mass-transit-systems-in-metro-manila-lrt-line-2-east-masinag-extension-project.html> last accessed July 19, 2019.*

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In reply, please be informed, as follows:

Tax Assumption Scheme

Under Section 7 of the Exchange of Notes which provides, to wit:

> "(1) The Government of the Republic of the Philippines shall, by itself or through its executing agency, assume:
>
> (a) all fiscal levies and taxes imposed in the Republic of the Philippines on JICA on and/or in connection with the Loan as well as interest accruing therefrom;
>
> (b) all duties and related fiscal charges imposed in the Republic of the Philippines on the Japanese companies operating as suppliers, contractors and/or consultants with respect to the import and re-export of their own materials and equipment needed for the implementation of the Project;
>
> (c) all fiscal levies and taxes imposed in the Republic of the Philippines on the Japanese companies operating as suppliers, contractors and/or consultants with respect to the payment carried out for and the income accruing from the supply of the products and/or services required for the implementation of the Projects; and
>
> (d) all fiscal levies and taxes imposed in the Republic of the Philippines on the Japanese employees engaged in the implementation of the Projects with respect to their personal income derived from Japanese companies operating as suppliers, contractors and/or consultants for the implementation of the Projects.
>
> (2) In connection with such tax assumption, the Government of the Republic of the Philippines or its executing agency shall be responsible for the liquidation or settlement of such fiscal levies, duties, taxes and other similar charges."

the Philippine Government shall, by itself or through its executing agency, assume:

a) all duties and related fiscal charges imposed in the Republic of the Philippines on the Japanese companies operating as suppliers and contractors with respect to the import and re-export of their own materials and equipment needed for the implementation of the Project;

b) all fiscal levies and taxes imposed in the Republic of the Philippines on the Japanese companies operating as suppliers and contractors with respect to the payment carried out for and the income accruing from the supply of the products and/or services required for the implementation of the Project; and

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c) all fiscal levies and taxes imposed in the Republic of the Philippines on the Japanese employees engaged in the implementation of the Project with respect to their personal income derived from Japanese companies operating as suppliers and contractors for the implementation of the Project.

Relative thereto, the Philippine Government or its executing agency shall be responsible for the liquidation or settlement of such fiscal levies, duties, taxes, and other similar charges.

The Exchange of Notes provides only a tax assumption mechanism, *i.e.*, the obligation or liability to pay tax remains but the same is merely passed on to a different person. Consequently, income tax shall be imposed on the income of these Japanese companies operating as suppliers, contractors, or consultants and Japanese employees engaged in the implementation of the Project for the implementation of the Project; Value-added tax on every sale of goods and services related to the Project as well as the importation of their own materials and equipment needed for the Project; and income tax on the personal income of Japanese employees working on the Project. These taxpayers shall not however, by the express terms of the Exchange of Notes, assume the payment of these taxes.

In the Supreme Court case *Mitsubishi Corporation vs. Commissioner of Internal Revenue, G.R. No. 175772 dated June 5, 2017*, the Supreme Court discussed the concept of the 'tax assumption scheme,' citing the Supreme Court case of *Plaridel Abaya vs. Hon. Ebdane (DPWH), G.R. No. 167919 dated February 14, 2007* and Paragraph 5 (2) of the Exchange of Notes:

> "An *"exchange of notes"* is a record of a routine agreement that has many similarities with the private law contract. The agreement consists of the exchange of two documents, each of the parties being in the possession of the one signed by the representative of the other. Under the usual procedure, the accepting State repeats the text of the offering State to record its assent. The signatories of the letters may be government Ministers, diplomats or departmental heads. The technique of exchange of notes is frequently resorted to, either because of its speedy procedure, or, sometimes, to avoid the process of legislative approval.
>
> It is stated that "treaties, agreements, conventions, charters, protocols, declarations, memoranda of understanding, modus vivendi and exchange of notes" all refer to "international instruments binding at international law.
>
> x x x x
>
> Significantly, an exchange of notes is considered a form of an executive agreement, which becomes binding through executive action without the need of a vote by the Senate or Congress
>
> Paragraph 5 (2) of the Exchange of Notes provides for a tax assumption provision whereby:
>
> *(2) <u>The Government of the Republic of the Philippines will, itself or through its executing agencies or instrumentalities, assume all fiscal levies or taxes imposed in the Republic of the Philippines on Japanese firms and nationals operating as suppliers, contractors or consultants on and/or in connection with any income that may accrue from the supply of products of Japan and services of Japanese nationals to be provided under the Loan.</u>"* (Emphasis supplied)

In the said case, the Supreme Court discussed what is to "assume," which is *"to take on, become bound as another is bound, or put oneself in place of another as to an obligation or liability.* It further provided that based on said definition, *"the obligation or liability remains, although the same is merely passed on to a different person. In this light, the concept of an assumption is therefore different from an exemption, the latter being the "[f]reedom from a duty, liability or other requirement" or "[a] privilege given to a judgment debtor by law, allowing the debtor to retain [a] certain property without liability."*

It therefore decided that in line with the tax assumption provision under the Exchange of Notes, the executing government agency, shall pay any form of taxes that are directly imposable under the Contract, as follows:

> "As explicitly worded, the Philippine Government, through its executing agencies (i.e., NPC in this case) particularly assumed "all fiscal levies or taxes imposed in the Republic of the Philippines on Japanese firms and nationals operating as suppliers, contractors or consultants on and/or in connection with any income that may accrue from the supply of products of Japan and services of Japanese nationals to be provided under the [OECF] Loan." The Philippine Government's assumption of "all fiscal levies and taxes," which includes the subject taxes, is clearly a form of concession given to Japanese suppliers, contractors or consultants in consideration of the OECF Loan, which proceeds were used for the implementation of the Project. As part of this, NPC entered into the June 21, 1991 Contract with Mitsubishi Corporation (i.e., petitioner's head office in Japan) for the engineering, supply, construction, installation, testing, and commissioning of a steam generator, auxiliaries, and associated civil works for the Project, which foreign currency portion was funded by the OECF loans. Thus, in line with the tax assumption provision under the Exchange of Notes, Article VIII (B) (1) of the Contract states that NPC shall pay any and all forms of taxes that are directly imposable under the Contract."

Accordingly, the DOTr shall assume all taxes, such as income tax (and consequently withholding tax thereto), value-added tax (and consequently withholding tax thereto), and other taxes in relation to the Project, and all fiscal levies on the projects herein mentioned pursuant to the tax assumption scheme in compliance of the provisions of the Exchange of Notes. *(Mitsubishi Corporation vs. Commissioner of Internal Revenue, G.R. No. 175772 dated June 5, 2017).*

Liability for Income Taxes

The applicable income taxes in this case includes corporate income tax (CIT) of the UC and Japanese companies operating as suppliers and contractors, personal income tax (PIT) of Japanese employees engaged in the implementation of the Project, fringe benefits tax (FBT) of qualified Japanese employees other than rank and file. Under normal circumstances, the CIT is the direct liability of the Japanese companies operating as suppliers and contractors, while the FBT and PIT are direct liabilities of the income recipients themselves but are required to be withheld at source. Under the Exchange of Notes however, these income taxes are the liabilities of the DOTr under the Exchange of Notes.

Accordingly, the UC, an unincorporated consortium having been formed solely for the purpose of bidding, implementing, and the construction of the LRT Line 2 – East (Masinag) Extension Project under the Contract for Procurement of Trackwork, Electrical and Mechanical (E&M) Systems and Integration with Existing Systems for LRT Line 2 – East (Masinag) Extension Project with the Department of Transportation (DOTr), is subject to the corporate income tax, through the UC members, provided that the lead partner is Marubeni and that its scope of work is more than 50% of the contract amount. Pursuant, however, to the Exchange of Notes between the Government of Japan and the Government of the Republic of the Philippines, this income tax on the Japanese companies shall be assumed by DOTr.

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By reason of such tax assumption scheme, pursuant to the Exchange of Notes, income payments made by the DOTr to the UC are not subject to the 2% CWT prescribed under Section 57(B) of the Tax Code, as amended, as implemented by Revenue Regulations (RR) No. 2-98, as amended by RR No. 11-2018, provided that the lead partner is Marubeni and that its share of work is more than 50% of the contract amount. Under the tax assumption scheme, the DOTr shall assume the 2% CWT (if any), on the Japanese company.

While the payment of these taxes is assumed by the Philippine Government or DOTr pursuant to the Exchange of Notes, the computation thereof, the filing of return and remittance (where applicable) to the BIR shall still be the duty of the consortium members. It must be emphasized that the amount of these taxes could be determined only by the consortium members after taking into account the gross income derived from the Project and allowable deductions (ordinary and necessary expenses paid or incurred during the taxable year which are directly attributable to the implementation of the Project) when ascertaining the liability for corporate income tax; the net taxable compensation for PIT; and the grossed-up monetary value of the fringe benefit for FBT. These amounts are supported by sufficient evidence, such as official receipts, invoices or other adequate records, which are under the possession and custody of the UC and/or the consortium members. Hence, only the UC and/or the consortium members could accurately determine the amount of taxes to be shouldered by the Philippine government or its implementing agency and could supply the information needed for the preparation of returns. Moreover, only the assumption of taxes was passed on to the DOTr under the Exchange of Notes and not the reporting obligations with the BIR.

Value Added Tax

Revenue Memorandum Circular (RMC) No. 8-2017 (Re: Clarifying the Tax Treatment of Value-Added Tax on Government Money Payments for OECF Funded Projects under Exchange of Notes Between Republic of the Philippines and the Government of Japan"), provides that in order to implement the tax assumption scheme under the Exchange of Notes, the following rules shall govern for VAT purposes:

1. *"The VAT-registered suppliers and sub-contractors of the Japanese companies shall bill and pass on the twelve percent (12%) VAT to the Japanese companies/contractors. In turn, the Japanese contractors shall include in their billing and pass on the 12% VAT to the concerned executing agencies of the Republic of the Philippines. Since under the Exchange of Notes, the OECF Fund shall not be used to pay for the tax, then the VAT is for the account of the Philippine government.*

2. *The Japanese contractors shall file the prescribed VAT returns on gross receipts derived from OECF-funded projects, claim their input taxes from their purchase of goods, properties and services from their suppliers or subcontractors and shall pay the output tax or VAT thereon, after offsetting the creditable or allowable input taxes, considering that the amount intended for payment of the VAT has already been collected and received by the Japanese contractors or nationals from the executing government agencies as part of the total billing/invoice price.*

3. *In no case shall input taxes arising from transactions attributable to activities unrelated to the OECF-funded project be allowed or be credited against the output tax on gross receipts from the project."*

Pursuant to RMC No. 8-2017, the VAT-registered suppliers and sub-contractors of the UC shall bill and pass on the twelve percent (12%) VAT to the UC. In turn, the UC shall include in its billing and pass on the twelve percent (12%) VAT to the DOTr. Since under the Exchange of Notes, the DOTr shall assume the payment of taxes, then the VAT is for the

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account of DOTr. Moreover, the Japanese contractors, shall file the prescribed VAT returns on gross receipts derived from the JICA-funded Project, claim its input taxes from its purchases of goods, properties, and services and shall pay the output tax thereon, after offsetting the creditable or allowable input taxes, considering that the amount intended for the payment of the VAT has already been collected and received by UC from the DOTr as part of its billing. Therefore, the UC is allowed to bill and seek the payment of the 12% VAT paid in connection with the Project from DOTr. The DOTr shall not, however, withhold a final VAT of 5% [now creditable under R.A. No. 10963 beginning January 1, 2021] before making payments to the UC since it is obligated under the exchange of Notes to assume the payment of the 12% VAT.

In no case, however, shall input taxes arising from transactions attributable to activities unrelated to the Project shall be allowed or be credited against the output tax on gross receipts from the Project.

Value Added Tax on Importation of Materials and Equipment

Section 107 (A) of the Tax Code, as amended, imposes the VAT on importation on the importer of record:

> *"SECTION 107. Value-added Tax on Importation of Goods. —*
>
> *(A) In General. — There shall be levied, assessed and collected on every importation of goods a value-added tax equivalent to twelve percent (12%) based on the total value used by the Bureau of Customs in determining tariff and customs duties, plus customs duties, excise taxes, if any, and other charges, <u>such tax to be paid by the importer prior to the release of such goods from customs custody</u>: Provided, That where the customs duties are determined on the basis of the quantity or volume of the goods, the value-added tax shall be based on the landed cost plus excise taxes, if any."* (Underscoring ours)

The DOTr, as the importer of record, is therefore liable for the 12% VAT on importations. Even assuming that the UC is liable for the said tax, the 12% VAT on importation imposed under Section 107 (A) of the Tax Code, as amended, shall likewise be assumed by the DOTr as discussed under the tax assumption scheme and pursuant to the holding of the Supreme Court in *Mitsubishi Corporation – Manila Branch vs. Commissioner of Internal Revenue (G.R. No. 175772 dated June 5, 2017).*

VAT on importation by the Japanese companies operating as suppliers and contractor of their own materials and equipment needed for the implementation of the Project shall likewise be assumed by the DOTr.

Payments to Japanese personnel and its Japanese contractors

Pursuant to the Particular Conditions and the Exchange of Notes deemed considered part of the Contract Agreement, and pursuant to the holding in Supreme Court in *Mitsubishi Corporation – Manila Branch vs. Commissioner of Internal Revenue (G.R. No. 175772 dated June 5, 2017)*, the personal income tax of the Japanese personnel employed by the UC and its Japanese contractors performing work in the Philippines shall likewise be assumed by the DOTr pursuant to the tax assumption scheme. The Japanese personnel employed by the UC and its Japanese contractors performing work in the Philippines pursuant to the JICA-funded Project are required to file income tax returns but the DOTr shall assume the payment of the aforesaid taxes. *(BIR Ruling DA-244-06 dated April 12, 2006).*

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Implementation of the Tax Assumption Scheme

After the determination of the income taxes, the Japanese companies operating as suppliers, contractors, or consultants and Japanese employees engaged in the implementation of the Project, shall immediately prepare the tax returns and necessary documents, particularly the official receipts and/or invoices, other relevant accounting records, and proceed to the DOTr to secure the payment of these taxes. The implementing agency, on the other hand, shall immediately evaluate the documents submitted and prepare whatever document is necessary for the release of funds allocated for the payment of these taxes. Penalties for late filing shall likewise be assumed by the implementing agency since liability thereto attaches to the person directly liable for the payment of taxes. Therefore, to avoid penalties, the implementing agency shall observe the deadline for the payment of taxes and the Japanese companies operating as suppliers, contractors, or consultants and Japanese employees engaged in the implementation of the Project shall give the former sufficient time to evaluate the documents and returns submitted to it.

SUCH BEING THE CASE, the Republic of the Philippines or through its executing agency (*i.e.*, DOTr) shall assume all taxes, duties, and related fiscal charges to be imposed on the UC, including, Japanese suppliers, contractors, and personnel engaged in the LRT Line 2 – East (Masinag) Extension Project under the Contract for Procurement of Trackwork, Electrical and Mechanical (E&M) Systems and Integration with Existing Systems for LRT Line 2 – East (Masinag) Extension Project, provided that the supply of goods and/or services and other activities of the said suppliers, contractors, and personnel bear a direct connection to the LRT Line 2 – East (Masinag) Extension Project under the Contract for Procurement of Trackwork, Electrical and Mechanical (E&M) Systems and Integration with Existing Systems for LRT Line 2 – East (Masinag) Extension Project.

Stated otherwise, all taxes directly associated with the Project, shall be assumed by the executing government agency and collected by the BIR from the executing government agency.

Accordingly, we hereby confirm your opinion that:

1. The unincorporated consortium, Marubeni-DMCI Consortium (hereinafter "UC"), having been formed solely for the purpose of bidding and implementing the LRT Line 2 – East (Masinag) Extension Project under the Contract for Procurement of Trackwork, Electrical and Mechanical (E&M) Systems and Integration with Existing Systems for LRT Line 2 – East (Masinag) Extension Project with the Department of Transportation (DOTr), is subject to the corporate income tax, through the UC members, provided that the lead partner is Marubeni and that its share of work is more than 50% of the contract amount. However, pursuant to the Exchange of Notes between the Government of Japan and the Government of the Republic of the Philippines, the said income tax on the Japanese company shall be assumed by DOTr;

2. By reason of such tax assumption scheme, the gross payments made by DOTr to the UC are not subject to the 2% creditable withholding tax (CWT) under Section 57 (B) of the Tax Code, as amended and implemented by Revenue Regulations No. 2-98, as amended by Revenue Regulations No. 11-2018;

3. Since this is only tax assumption scheme, the UC, through its members, is still required to file quarterly and annual income tax returns with BIR;

4. On the VAT aspect of the project, pursuant to the holding of the Supreme Court in *Mitsubishi Corporation – Manila Branch v. Commissioner of Internal Revenue (G.R. No. 175772 dated June 5, 2017)* and *Revenue Memorandum Circular (RMC) No. 8-2017*:

    a. The VAT-registered suppliers and sub-contractors of the UC shall bill and pass on the twelve percent (12%) VAT to the UC. In turn, the UC shall include in its billing

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and pass on the twelve percent (12%) VAT to the DOTr. Since under the Exchange of Notes, the DOTr shall assume the payment of taxes, then the VAT is for the account of DOTr;

b. The Japanese contractors, shall file the prescribed VAT returns on gross receipts derived from the JICA-funded Project, claim its input taxes form its purchases of goods, properties, and services and shall pay the output tax thereon, after offsetting the creditable or allowable input taxes, considering that the amount intended for the payment of the VAT has already been collected and received by UC from the DOTr as part of its billing;

5. As the importer of record, the DOTr shall be liable for the 12% VAT on the importation of materials and equipment under Section 107(A) of the Tax Code, as amended;

6. The Japanese personnel employed by the UC and its Japanese contractors performing work in the Philippines pursuant to the JICA-funded Project are required to file income tax returns but the DOTr shall assume the payment of the taxes due thereunder. Accordingly, the said Japanese personnel are not subject to withholding tax on compensation under Section 57 of the Tax Code, as amended, pursuant to the tax assumption provisions under the Exchange of Notes and the holding of the Supreme Court in *Mitsubishi Corporation – Manila Branch v. Commissioner of Internal Revenue (G.R. No. 175772 dated June 5, 2017).*

7. In connection with the tax assumption scheme and pursuant to the Exchange of Notes, the Government of the Republic of the Philippines or its executing agency (i.e., Department of Transportation) shall be responsible for the liquidation or settlement of such fiscal levies, duties, taxes, and other similar charges.

This ruling is being issued on the basis of the foregoing facts as represented. However, if upon investigation, it will be disclosed that the facts as represented are different, then this ruling shall be considered null and void.

Very truly yours,

CAESAR R. DULAY
Commissioner of Internal Revenue

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