REPUBLIC OF THE PHILIPPINES
DEPARTMENT OF FINANCE
BUREAU OF INTERNAL REVENUE

Quezon City

Secs. 23 (F), 28(B)(1), 42(C)(3); and 108, Tax Code, as amended
BIR Ruling No. 457-14
CT- 358-2[illegible]
OCT [illegible]

E.C. Baligod Law Office
25-B Lanzones Street
Quirino 2-A, Project 2
Quezon City

Attention: **Atty. Emilio C. Baligod**

Gentlemen:

This refers to your letter dated August 6, 2018 requesting on behalf of your client, Yang Seop Lee, representative of **Hanwha Corporation ("Hanwha Corp.")** and **Hanwha Techwin Co. Ltd. ("Hanwha Tech.")**, for a confirmation of your opinion that the payments made by the Armed Forces of the Philippines (**"AFP"**) to Hanwha Corp. and Hanwha Tech. relative to three (3) Contracts for the procurement of Rocket Motor, HE and Rocket Motor and Inert are exempt from withholding tax, being payment for services rendered outside the Philippines in accordance with Section 28 (B) (1) of the National Internal Revenue Code of 1997 (Tax Code), as amended.

As represented, Hanwha Corp. and Hanwha Tech. are non-resident foreign corporations duly organized under the laws of the Republic of Korea (South Korea) not licensed to engage in business in the Philippines. Hanwha Corp. and Hanwha Tech. are engaged in manufacturing, supplying and selling military hardware, ammunition, etc. to the Philippines.

Hanwha Corp. in joint venture with Hanwha Tech., represented by its Authorized Representative, Mr. Yang Seop Lee, with address at #86, Cheonggyecheon-to Jung-gu, Seoul, South Korea, won in the public bidding of three (3) Contracts to provide goods (Rocket Motor, HE and Rocket Motor, Inert), services and to remedy defects therein in conformity in all respects with the provisions of the Contract. After full delivery of the products, the AFP Philippine Airforce Procurement Center, Procurement Service is imposing 30% withholding tax on the purchase price of military hardware on the ground that it is an income gained by Hanwha Corp. and Hanwha Tech. in the Philippines as defined by Section 28 (B) (1) of the Tax Code, as amended.

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In reply, please be informed that Section 22 (H) and (I) of the National Internal Revenue Code of 1997 (Tax Code), as amended, defines resident and non-resident foreign corporations as follows:

"Section 22. Definitions. – when used in this Title:

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(H) The term ***'resident foreign corporation'*** *applies to a foreign corporation engaged in trade or business within the Philippines.*

(I) The term ***'non-resident foreign corporation'*** *applies to a foreign corporation not engaged in trade or business within the Philippines."*

Based on the above definitions, a foreign corporation, while its offices may be located abroad, becomes a resident of the Philippines when it engages in trade or business within the Philippines. The test therefore in determining whether or not a foreign corporation is a resident of the Philippines, for purposes of taxation, is not the physical location of its offices but the presence of its business activities within the Philippines. (BIR Ruling No. 457-14 dated November 12, 2014)

Thus, while it is true that Hanwa Corp. and Hanwa Tech hold offices in South Korea, it is still considered engaged in trade or business in the Philippines when it participated in the bidding process conducted by the AFP in the Philippines for the procurement of the subject equipment, thereby qualifying it as a resident foreign corporation under Section 22 (H) of the Tax Code, as amended.

As held by the Supreme Court in Accenture, Inc. vs. CIR, G.R. No. 190102, July 11, 2012), to wit:

"There is no specific criterion as to what constitutes 'doing' or 'engaging in' or 'transacting' business. We ruled thus in Commissioner of Internal Revenue v. British Overseas Airways Corporation:

. . . . There is no specific as to what constitutes 'doing' or 'engaging' or 'transacting' business. Each case must be judged in the light of its peculiar environmental circumstances. The term implies a continuity of commercial dealings and arrangements, and contemplates, to that extent, the performance of acts or works or the exercise of some of the functions normally incident to, and in progressive prosecution of commercial gain or for the purpose and object of the business organization. In order that a foreign corporation may be regarded as doing business within a State, there must be continuity of conduct and intention to establish a continuous business, ***such as the appointment of a local agent****, and not one of a temporary character." (Emphasis supplied)*

The appointment by the companies of a representative for them to participate in the bidding process of the AFP for the procurement of the equipment evinces their intention to do business in the Philippines.

Moreover, the contracts involved sale of goods (Rocket Motors) and not services. Section 42 (E) of the Tax Code, as amended, provides that gains, profits and income from the sale of personal property shall be treated as derived entirely from sources within the country in which the goods or property are sold. In this case, the goods are sold within the Philippines, the bidding process having been conducted, and the contracts for the procurement of the same having been executed, in the Philippines.

In view of the foregoing, the payment for the Rocket Motor, HE and Rocket Motor and Inert are subject to income tax, and consequently to withholding tax.

However, Section 10 of Republic Act (RA) No. 10349 which is the law applicable at the time of the transactions, provides:

> *"SEC. 10. Insert three (3) sections after Section 16 of the same Act which shall now become the new Sections 17, 18 and 19 respectively, which shall read as:*
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> > *'SEC. 17. Exemption from Value-Added Tax and Customs Duties. - The sale of weapons, equipment and ammunitions to the AFP, which are directly and exclusively used for its projects, undertakings, activities and programs under the Revised AFP Modernization Act, shall be exempt from the valued-added tax; Provided, That the importation of the same by the AFP shall likewise be exempt from the value-added tax and customs duties.'*
>
> *xxx xxx xxx"*

Under Section 10 of RA 10349, the sale of weapons, equipment and ammunitions to the Armed Forces of the Philippines (AFP), which are directly and exclusively used for its projects, undertakings, activities and programs under the Revised AFP Modernization Act, shall be exempt from the valued-added tax (VAT). Moreover, the importation of the same by the AFP shall likewise be exempt from the VAT. In relation thereto, the Department of National Defense (DND) issued the Department Circular No. 3 (Issuing the Implementing Guidelines, Rules and Regulations of the Revised Armed Forces of the Philippines Modernization Act) dated April 11, 2013 which, among others, defined the term "equipment" as referring to "*all non-expendable items needed to outfit or equip any individual and/or organizations and sub-organizations within the AFP.*"

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Therefore, the sale of military hardware to the AFP by Hanwha Corporation and Hanwha Techwin Co. Ltd., covered by Contract Agreements notarized on June 5 and 7, 2017, is not subject to VAT on the sale and importation of goods imposed in Sections 106 and 107 of the Tax Code, as amended, provided that the aforesaid Rocket Motor, HE and Rocket Motor and Inert shall be used directly and exclusively by the AFP for its projects, undertakings, activities and programs under the Revised AFP Modernization Act.

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 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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