REPUBLIC OF THE PHILIPPINES
DEPARTMENT OF FINANCE
BUREAU OF INTERNAL REVENUE

Quezon City

Republic Act No. 11506	

Date: ______________

SAN MIGUEL AEROCITY INC.
40 San Miguel Avenue
Mandaluyong City 1550

Attention: **Mariano Miguel L. Trinidad Jr.**
Comptroller

Gentlemen:

This refers to your request on behalf of **San Miguel Aerocity Inc.** ("**SMAI**"), requesting for the clarifications on the implementation of Sections 16 and 17 of Republic Act (RA) No. 11506, entitled "*THE ACT GRANTING SAN MIGUEL AEROCITY INC. A FRANCHISE TO CONSTRUCT, DEVELOP, ESTABLISH, OPERATE, AND MAINTAIN A DOMESTIC AND INTERNATIONAL AIRPORT IN THE MUNICIPALITY OF BULAKAN, PROVINCE OF BULACAN, AND TO CONSTRUCT, DEVELOP, ESTABLISH, OPERATE AND MAINTAIN AN ADJACENT AIRPORT CITY*", which became effective on January 15, 2021 – to wit:

> *"Section 16. Tax Exemptions. - During the ten-year construction period, the grantee, its successors or assignees, shall be exempt from any and all direct and indirect taxes and fees of any kind, nature or description, which emanate exclusively from the construction, development, establishment, and operation of the airport and Airport City, including income taxes, value-added taxes, percentage taxes, excise taxes, documentary stamp taxes, customs duties and tariffs, taxes on real estate, buildings and personal property, business taxes, franchise taxes, supervision fees, and permit fees levied, established or collected, or may be levied, established or collected, by any city, municipal, provincial or national authority.*
>
> *After the ten-year construction period and during the remaining term of this franchise, the grantee, its successors or assignees, shall be exempt from income taxes and taxes on real estate, buildings and personal property, levied, established or collected, or may be levied, established or collected, by any city, municipal, provincial or national authority. However, such exemption from income taxes and taxes on real estate, buildings and personal property shall expire as soon as it is determined by the Bureau of Internal Revenue (BIR) that the grantee, its successors or assignees, has fully recovered its investment cost on the airport and on the Airport City, whereupon the grantee, its successors or assignees, shall be subjected to all taxes under the National Internal Revenue Code of 1997, as amended, and the Customs Modernization and Tariff Act."*

As represented, the phrase "construction, development, establishment, and operation" include all transactions that are necessary, related or incidental to the undertaking of the construction, development, establishment, operation and maintenance of the Airport and Airport City, such as, but not limited to:

1. Sales of goods and services, and other income generating activities
2. Purchases and importation of goods and services
3. Engagement of contractors and consultants
4. Purchase and/or sale of real and personal properties
5. Lease of real and personal properties
6. Financing transactions
7. Foreign exchange transactions
8. Hedging transactions
9. Management and other operations

In reply, please be informed that this Ruling clarifies the implementation of the provisions on the Tax Exemptions (Section 16) of RA No. 11506 involving the franchise of SMAI ("Aerocity Franchise", for short). For purposes of this Ruling, SMAI, the grantee, shall necessarily include its successors or assignees.

It is provided under Section 16 of the Aerocity Franchise that during the Ten-Year Construction Period, SMAI shall be exempt from any and all direct and indirect taxes and fees of any kind, nature or description, which emanate exclusively from the construction, development, establishment, and operation of the Airport and Airport City, including income tax, value-added tax, percentage tax, excise tax, documentary stamp tax, customs duties and tariffs, taxes on real estate, buildings and personal property, business taxes, franchise taxes, supervision fees, and permit fees levied, established or collected, or may be levied, established or collected, by any city, municipal, provincial or national authority.

The internal revenue taxes shall be implemented in two phases such as (I) the Ten-Year Construction Period; and (II) after the Ten-Year Construction Period and during the remaining term of the Aerocity Franchise. The second phase, however, shall have two (2) sub-phases, such as (A) period of recovery; and (B) period after SMAI has fully recovered its Investment Cost on the Airport and on the Airport City.

I. DURING THE TEN-YEAR CONSTRUCTION PERIOD

During the Ten-Year Construction Period, which starts on 15 January 2021 (effective date of the Aerocity Franchise) and ends on 14 January 2031, SMAI shall be exempt from any and all direct and indirect taxes, duties, tariffs and fees of any kind, nature or description, which emanate exclusively from the construction, development, establishment, and operation of the Airport and Airport City, including income tax, value-added tax, percentage tax, excise tax and documentary stamp tax.

A. <u>Income Tax</u>

During the Ten-Year Construction Period, SMAI may generate income emanating exclusively from the construction, development, establishment, and operation of the Airport and Airport City. As provided under the Aerocity Franchise, such income is exempt from income tax.

Section 27 of the National Internal Revenue Code of 1997 (Tax Code), as amended, provides for the rate of the income tax on Domestic Corporations, to wit:

> *"Section 27 Rates of Income Tax on Domestic Corporations.*[1]
>
> (A) *In General. Except as otherwise provided in this Code, an income tax of twenty-five percent (25%) effective July 1, 2020, is hereby imposed upon the taxable income derived during each taxable year from all sources within and without the Philippines by every corporation, as defined in Section 22(B) of this Code and taxable under this Title as a corporation, organized in, or existing under the laws of the Philippines. xxx"*

However, the Aerocity Franchise expressly provides for income tax exemption of SMAI. Accordingly, during the Ten-Year Construction Period, the income of SMAI which emanates exclusively from the construction, development, establishment, and operation of the Airport and Airport City, is exempt from income tax. This income tax exemption SMAI shall inescapably include exemptions under Sections 27(D) and 27(E) of the Tax Code, as amended, to wit:

> *"(D) Rates of Tax on Certain Passive Incomes.*
>
> *xxx xxx xxx*
>
> *(E) Minimum Corporate Income Tax on Domestic Corporations.*
>
> *xxx xxx xxx"*

Moreover, please be informed that Section 2.57.5(B)(2) of the Revenue Regulations (RR) No. 2-98, as amended, provides as follows:

> *"SECTION 2.57.5. Exemption from Withholding. The withholding of creditable withholding tax prescribed in these Regulations shall not apply to income payments made to the following:*
>
> *xxx xxx xxx*
>
> *(B)* ***Persons enjoying exemption from payment of income taxes pursuant to the provisions of any law, general or special****, such as but not limited to the following: xxx"*

[1] As amended by R.A No. 11534, "An Act Reforming the Corporate Income Tax and Incentives System, amending for the purpose Sections 20,22,25,27,29,34,40,57,209 116,204 and 209 of the National Internal Revenue Code of 1997, as amended, and creating therein the new Title XIII and for other purposes

Based on the foregoing, Section 2.57.5 (B) of RR 2-98, as amended, is explicit in stating that the expanded withholding tax does not apply to income payments to persons enjoying exemption from payment of income taxes pursuant to the provisions of any law, general or special. Accordingly, since SMAI is exempt under the Aerocity Franchise, which is a special law, income payments to be made to it during the Ten-Year Construction Period is not subject to expanded withholding tax prescribed under RR. No. 2-98, as amended.

It must be emphasized, however, that the exemption from income tax granted to SMAI does not extend to its local or non-resident suppliers of goods, property or services. Accordingly, SMAI, as a constituted withholding agent for the government, is required to withhold the withholding tax on income payments to persons subject to tax pursuant to Section 57 of the Tax Code, as amended. Provided, however, that in the case of non-resident suppliers, the applicable final withholding tax may be reduced or eliminated under relevant tax treaty provisions, subject to compliance with applicable tax laws, rules and regulations.

B. <u>Value-Added Tax ("VAT")</u>

As regards the VAT exemption of SMAI, Section 109 (1) (K) of the Tax Code, as amended, provides:

> *"Section 9. Exempt Transactions – (1) Subject to the provisions of Subsection (2) hereof, the following transactions shall be exempt from the value-added tax:*
>
> *xxx xxx xxx*
>
> *(K) Transactions which are exempt under international agreements to which the Philippines is a signatory or* ***under special laws,*** *except those under Presidential Decree No. 529" (emphasis supplied)*

Accordingly, since the Aerocity Franchise, which is a special law, expressly exempts SMAI from VAT, its sales of goods, property and services during the Ten-Year Construction Period, which emanate exclusively from the construction, development, establishment, and operation of the Airport and Airport City, shall not be subject to VAT.

Moreover, Section 106(A)(2)(b) of the Tax Code, as amended, provides for VAT at zero rate on sales to entities exempt under special laws, to wit:

> *"Section 106. Value-Added Tax on Sale of Goods or Properties. -*
>
> *A) Rate and Base of Tax. - There shall be levied, assessed and collected on every sale, barter or exchange of goods or properties, a value-added tax equivalent to twelve percent (12%) of the gross selling price or gross value in money of the goods or*

properties sold, bartered or exchanged, such tax to be paid by the seller or transferor.

xxx xxx xxx

(2) The following sales by VAT-registered persons shall be subject to zero percent (0%) rate:

xxx xxx xxx

*(b) **Sales to persons or entities whose exemption under special laws** or international agreements to which the Philippines is a signatory effectively subjects such sales to zero rate."* (emphasis supplied)

Relatively, Section 108(B)(3) of the Tax Code, as amended, provides for VAT at zero rate on services rendered to entities exempt under special laws, to wit:

"Section 108. Value-added Tax on Sale of Services and Use or Lease of Properties. –

xxx xxx xxx

B) Transactions Subject to Zero Percent (0%) Rate. – The following services performed in the Philippines by VAT-registered persons shall be subject to zero percent (0%) rate:

xxx xxx xxx

*(3) **Services rendered to persons or entities whose exemption under special laws** or international agreements to which the Philippines is a signatory **effectively subjects the supply of such services to zero percent (0%) rate:**"* (emphasis supplied)

Accordingly, as SMAI is exempt from any and all direct and indirect taxes, duties, tariffs and fees of any kind, nature or description under the Aerocity Franchise, all importations and domestic purchases of goods, property and services during the Ten-Year Construction Period, emanating exclusively from the construction, development, establishment, and operation of the Airport and Airport City, shall not be subject to VAT. Effectively, no VAT shall be passed on to SMAI on its importations and domestic purchases of goods and services emanating from the said activities for the Ten-Year Construction Period. This Ruling shall serve as sufficient basis and certification of SMAI's VAT exemption and for SMAI's VAT-registered suppliers of goods, property or services to treat their sales to SMAI as VAT-zero rated. No separate confirmatory ruling or certification is necessary for the suppliers of SMAI.

C. <u>Percentage Tax</u>

Under Section 16 of the Aerocity Franchise, SMAI shall be exempt from any and all direct and indirect taxes, including Percentage Tax. Accordingly, the sales or receipts of SMAI which emanate exclusively from the construction, development, establishment, and operation of the Airport and Airport City, is not subject to Percentage Tax imposed under Title V of the Tax Code, as amended.

D. Excise Tax

Under Section 16 of the Aerocity Franchise, SMAI shall be exempt from any and all direct and indirect taxes, including Excise Tax. Accordingly, all excisable transactions including importation of goods of SMAI which emanate exclusively from the construction, development, establishment, and operation of the Airport and Airport City, is not subject to Excise Tax imposed under Title VI of the Tax Code, as amended.

E. Documentary Stamp Tax (DST)

Under Section 16 of the Aerocity Franchise, SMAI shall be exempt from any and all direct and indirect taxes, including DST. Accordingly, SMAI is not subject to DST imposed under Title VII of the Tax Code, as amended, upon documents, instruments, loan agreements and papers, which emanate exclusively from the construction, development, establishment, and operation of the Airport and Airport City.

However, Section 173 of the Tax Code, as amended, provides as follows:

> *"Section 173. Stamp Taxes Upon Documents, Loan Agreements, Instruments and Papers. -- Upon documents, instruments, loan agreements and papers, and upon acceptances, assignments, sales and transfers of the obligation, right or property incident thereto, there shall be levied, collected and paid for, and in respect of the transaction so had or accomplished, the corresponding documentary stamp taxes prescribed in the following Sections of this Title, by the person making, signing, issuing, accepting, or transferring the same wherever the document is made, signed, issued, accepted or transferred when the obligation or right arises from Philippine sources or the property is situated in the Philippines, and the same time such act is done or transaction had:* ***Provided, That whenever one party to the taxable document enjoys exemption from the tax herein imposed, the other party thereto who is not exempt shall be the one directly liable for the tax."*** *(emphasis supplied)*

Thus, considering that SMAI enjoys exemption from the DST, the other party to the taxable document who is not exempt shall be the one directly liable to the DST imposed under Title VII of the Tax Code, as amended.

F. Donor's Tax

Under Section 16 of the Aerocity Franchise, SMAI shall be exempt from any and all direct and indirect taxes, including Donor's Tax. Accordingly, the donations made by SMAI which emanate exclusively from the construction, development, establishment, and operation of the airport and Airport City, is not subject to Donor's Tax imposed under Title III, Chapter II of the Tax Code, as amended.

G. **All other internal revenue taxes**

As provided under Section 16 of the Aerocity Franchise, SMAI shall be exempt from any and all direct and indirect taxes levied, established or collected, or may be levied, established or collected, by any city, municipal, provincial or national authority. Accordingly, SMAI is not subject to any other internal revenue taxes, which emanate exclusively from the construction, development, establishment, and operation of the Airport and Airport City.

At the start of, and during the, Ten-Year Construction Period, the BIR Certificate of Registration ("COR") of SMAI shall be updated such that it reflects the tax exemptions granted by the Aerocity Franchise.

II. AFTER THE TEN-YEAR CONSTRUCTION PERIOD

It is provided under the second paragraph of Section 16 of the Aerocity Franchise, that after the Ten-Year Construction Period and during the remaining term of this franchise, the grantee, its successors or assignees, shall be exempt from income taxes and taxes on real estate, buildings and personal property, levied, established or collected, or may be levied, established or collected, by any city, municipal, provincial or national authority. However, such exemption from income taxes and taxes on real estate, buildings and personal property shall expire as soon as it is determined by the Bureau of Internal Revenue (BIR) that the grantee, its successors or assignees, has fully recovered its investment cost on the airport and on the Airport City, whereupon the grantee, its successors or assignees, shall be subjected to all taxes under the National Internal Revenue Code of 1997, as amended, and the Customs Modernization and Tariff Act.

A. After the Ten-Year Construction Period and During the Term of the Franchise **but Before** the Full Recovery of the Investment Cost on the Airport and on the Airport City

After the Ten-Year construction period and during the term of the franchise **but before** the full recovery of the investment cost on the Airport and on the Airport City, SMAI shall continue to enjoy the exemption from income tax, as stated under Sec. 16 of the Aerocity Franchise.

B. After the Ten-Year Period and During the Term of the Franchise, **and After** the Full Recovery of the Investment Cost on the Airport and on the Airport City

After the Ten-Year Construction Period, during the term of the franchise, **and after** the Full Recovery of the Investment Cost on the Airport and on the Airport City, all the tax exemptions of SMAI shall expire. Accordingly, SMAI shall be subject to all taxes imposed under the Tax Code, amended.

In the event of the sale/transfer/assignment of rights and privileges including the tax exemptions as approved by Congress and set forth in Sections 14 and 16 of the Aerocity Franchise, SMAI is required to officially notify the BIR in writing of the same within sixty

(60) days from the execution thereof and attaching copies of the Deeds of Sale/Transfer/Assignment thereto, as the case may be. An updated Certificate of Registration and General Information Sheet shall also be submitted showing the relationship of the successor/transferee/assignee to SMAI and reflecting the rights, privileges and tax exemptions subject of the sale/transfer/assignment and granted under the Aerocity Franchise. The BIR may require the submission of additional documents relative to the updating of the Certificate of Registration.

For purposes of sale/transfer/assignment of rights and privileges relative to the construction, acquisition, ownership, leasing, operation, development or management of the Airport City in favor of an "affiliate" under Section 14 of the Aerocity Franchise, the term "affiliate" shall pertain to any entity whose "controlling interest is owned" by SMAI's parent corporation, San Miguel Corporation. The terms "affiliate" and "control" shall be governed by existing laws[i] as well as relevant BIR[ii] and SEC issuances[iii].

This Ruling shall serve as a Certification or confirmation of the tax exemptions of SMAI, its successors and assignees, as provided under R.A. 11506 or the Aerocity Franchise which took effect on January 15, 2021.

This Ruling is being issued on the basis of the facts and documents as represented and submitted. However, if upon investigation, the BIR ascertains 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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[i] Sec. 3, Item (b) of RA No. 9856 provides: "Affiliate" means a corporation that directly or indirectly, through one or more intermediaries, is controlled by, or is under the common control of another corporation, which thereby becomes its parent corporation.

Sec. 4, Item (b) RA No. 10142 provides: "Affiliate" shall refer to a corporation that directly or indirectly, through one or more intermediaries, is controlled by, or is under the common control of another corporation.

[ii] Section 3, Item 4 of RR No. 19-2020 provides: "Control" refers to the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities.

[iii] SEC Memorandum Circular 1-2020, Rule 3, Item c), provides: "Affiliate" means a corporation that directly or indirectly, through one or more intermediaries, is controlled by, or is under the common control of, another corporation, which thereby becomes its parent corporation.

The 2015 Implementing Rules and Regulations of the Securities Regulation Code (RA 8799), Rule 3, Item 3.1.8, provides: "Control" is the power to determine the financial and operating policies of an entity in order to benefit from its activities. It is presumed to exist when the parent entity owns, directly or through subsidiaries and/or associates, more than fifty percent (50%) of the voting power of an entity.