REPUBLIC OF THE PHILIPPINES
DEPARTMENT OF FINANCE
BUREAU OF INTERNAL REVENUE

Quezon City

Bureau of Internal Revenue Ruling

Section 114, NIRC, as amended Section 4.114(2)(a) of RR No. 16-2005 as amended by RR No. 04-2007		#356-2017

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

Date: August 8, 2017

LOS CONTRATISTAS DELA CIUDAD DE ZAMBOANGA
Veterans Avenue
(Beside Caltex Station)
Zamboanga City, 7000

Attn: **MANUEL L. VERAR JR.**
President

Sir:

This refers to your letter dated February 2, 2017 received by this office on February 22, 2017, requesting for a definitive ruling on what is the correct Value Added Tax (VAT) rate applicable in the preparation of Program of Works (POW) and Approved Budget of the Contract (ABC) of Government infrastructure projects in connection with Department Order (D.O.) No. 197 dated October 17, 2016[1] issued by the Department of Public Works and Highways (DPWH) which set the computation of the Value Added Tax (VAT) component for the preparation by the DPWH of ABC at five (5) percent.

Section B.5 of D.O 197 states that the VAT Component as an Indirect Cost shall be 5% of the sum of the estimated direct cost (EDC); overhead, contingencies and miscellaneous (OCM) and the profit.

In connection therewith, please be informed that sales to the government or any of its political subdivisions, instrumentalities or agencies including government-owned or controlled corporations (GOCCs), of goods and/or services are generally subject to the twelve percent (12%) VAT under Sections 106 and 108 of the NIRC, unless the sale transaction is specifically VAT-exempt or VAT zero-rated under the provisions of the NIRC or other special laws.

The rules on the collection and remittance of VAT on government purchases that are subject to VAT are prescribed under Section 4.114(2)(a) of Revenue Regulations (RR) No. 16-2005, implementing Section 114(C) of the National Internal Revenue Code (NIRC), to wit:

"SEC. 4.114-2. Withholding of VAT on Government Money Payments xxx.-

(a) The government or any of its political subdivisions, instrumentalities or agencies including government-owned or controlled corporations (GOCCs) shall, before making payment on account of each

[1] Revised Guidelines in the Preparation of Approved Budget for the Contract (ABC) previously prescribed under Department Order No. 22, Series of 2015

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> *purchase of goods and/or of services taxed at twelve percent (12%) VAT pursuant to Secs. 106 and 108 of the Tax Code, deduct and withhold a final VAT due at the rate of five percent (5%) of the gross payment thereof.*
>
> *The five percent (5%) final VAT withholding rate shall represent the net VAT payable of the seller. The remaining seven percent (7%)[2] effectively accounts for the standard input VAT for sales of goods or services to government or any of its political subdivisions, instrumentalities or agencies including GOCCs in lieu of the actual input VAT directly attributable or ratably apportioned to such sales. Should actual input VAT attributable to sale to government exceeds seven percent (7%) of gross payments, the excess may form part of the sellers' expense or cost. On the other hand, if actual input VAT attributable to sale to government is less than seven percent (7%) of gross payment, the difference must be closed to expense or cost. (Underscoring supplied)*

While government purchases are subject to the 12% VAT, the procuring government entity is only required to deduct and withhold a five percent (5%) final VAT based on the gross payment thereof. The 5% final VAT represents the net VAT that is payable by the seller of goods or services. The remaining seven percent (7%) would effectively account for the standard input VAT for the sale of goods/services to the government entity, in lieu of the actual input VAT directly attributable or ratably apportioned to such sale. The difference between the 7% VAT and the actual input tax incurred may form part of the sellers' expense or cost or will be closed to expense or cost, as the case may be.

As such, the appropriate VAT rate to be used in the preparation of the ABC is 12%. This is to allow the sellers of goods/services to have the 7% as their standard input VAT which is in lieu of the actual input VAT directly attributable or ratably apportioned to their sales to the government. It must be noted that sellers of goods and/or services to the government are not allowed to deduct the actual input VAT attributable to such sales against the output VAT on their regular sales because the 7% standard input VAT is supposed to take the place of said actual input VAT. Moreover, the actual input VAT attributable to sales to government cannot be claimed for refund or tax credit because Section 4.114-2(a) of RR No. 16-2005 already provides for the rule on how the sellers of goods/services can recoup the actual input VAT attributable or ratably apportioned to their sales to the government.

In view of the foregoing, the appropriate VAT rate to be used by the DPWH in the preparation of the ABC and POW is 12%.

This ruling is being issued on the basis of the foregoing facts as represented. However, if upon investigation, it will be ascertained 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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[2] As amended by Revenue Regulations No. 04-2007.