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

Secs. 23 (F) , 42 (A) (3), (C) (3), and 108 (A), all of the National Internal Revenue Code of 1997, as amended
BIR Ruling No. 068-2013
017-2018
1-17-2018

STEAG STATE POWER, INC.
20th Floor, Yuchengco Tower, RCBC Plaza
6819 Ayala Ave. cor. Sen. Gil Puyat Ave.
Makati City

Attention: JOY MARIA SOCORRO B. PAMINTUAN
Chief Finance Officer

Gentlemen:

This refers to your letter dated April 22, 2014, requesting for confirmation that the service fees to be paid by STEAG State Power Inc. ("SPI" for brevity) to STEAG GmbH ("GmbH" for brevity), a non-resident foreign corporation based in Germany, for SAP software maintenance services to be rendered outside the Philippines is not subject to Philippine income tax and consequently to withholding tax as well as the 12% value-added tax (VAT).

Background:

SPI with TIN , is a corporation duly organized and existing under the laws of the Philippines. It is primarily engaged in the business power generation and subsequent sale of said generated power to the National Power Corporation (NPC) under a Build, Operate and Transfer (BOT) Scheme. It is registered with the Board of Investments (BOI) as a New Operator of 200 MW Coal Fired Power Generating Plant per BOI Certificate of Registration No. 97-078.

On the other hand, GmbH is a company duly incorporated and existing under the laws of Germany with its principal office at Ruttenscheider Str. 1-3, 45128 Essen, Germany. GmbH is not registered either as a corporation or as a partnership in the Philippines, as shown in the Certification of Non-Registration of Company issued by the Securities and Exchange Commission on March 12, 2014.

On February 18, 2014, SPI and GmbH entered into a SAP Software Maintenance Service Agreement ("Service Agreement") wherein GmbH will provide support on SPI's SAP Software. As described in Schedule I of page 6 of the Service Agreement, GmbH will provide the following services:

1. Operation of a SAP system as a client of STEAG ERP Systems;
2. Customizing of SAP software modules and system adjustments; and
3. Coordination and support.

Under the terms of the Service Agreement, GmbH will render the above-described services entirely outside of the Philippines from Germany via a secured internet Virtual Private Network (VPN). No employee or GmbH will be sent to the Philippines to perform any of the said services. For services rendered, SPI will pay a fixed fee of EUR per month (collectively referred to as "Services Fees").

In reply, please be informed that under Section 23 (F) of the National Internal Revenue Code of 1997, as amended, a foreign corporation, like GmbH, whether or not engaged in trade

or business in the Philippines, is subject to income tax only with respect to income derived from sources in the Philippines, to wit:

> *"SEC. 23. General Principles of Income Taxation in the Philippines. - Except when otherwise provided in this Code:*
>
> *xxx xxx xxx*
>
> *(F) **A foreign corporation**, whether engaged or not in trade or business in the Philippines, **is taxable only on income derived from sources within the Philippines.**"* (Emphasis and underscoring supplied)

Concerning income from the provision of services, under Sections 42 (A) (3) and (C) (3) of the National Internal Revenue Code of 1997, as amended, income is considered derived in the Philippines only if the services are actually performed in the Philippines, to wit:

> *"SEC. 42. Income from Sources Within the Philippines. –*
>
> *(A) Gross Income from Sources Within the Philippines. - The following items of gross income shall be treated as gross income from sources within the Philippines:*
>
> *xxx xxx xxx*
>
> *(3) Services. - Compensation for **labor or personal services performed in the Philippines;***
>
> *xxx xxx xxx*
>
> *(C) Gross Income from Sources Without the Philippines. - The following items of gross income shall be treated as income from sources without the Philippines:*
>
> *xxx xxx xxx*
>
> *(3) Compensation for **labor or personal services performed without the Philippines;**"* (Emphasis and underscoring supplied)

In *Commissioner of Internal Revenue v. Marubeni Corporation*[1], the Supreme Court held that only services rendered in the Philippines under a single contract are subject to the taxing jurisdiction of the Philippines and consequently subject to Philippine income tax. The Supreme Court ruled in this wise:

> *"Clearly, the service of design and engineering, supply and delivery, construction, erection and installation, supervision, direction and control of testing and commissioning, coordination. . ." of two projects involved two taxing jurisdictions. These acts occurred in two countries — Japan and the Philippines. While the construction and installation work were completed within the Philippines, the evidence is clear that some pieces of equipment and supplies were completely designed and engineered in Japan. The two sets of ship unloader and loader, the boats and mobile equipment of the NDC project and ammonia storage tanks and refrigeration units were made and completed in Japan. They were already finished products when shipped to the Philippines. The other construction supplies listed under the offshore portion such as the steel sheets, pipes and structures, electrical and instrumental apparatus, these were not finished products when shipped to the Philippines. They, however, were likewise fabricated and manufactured by the sub-contractors in Japan. All*

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[1] G.R. No. 1-37377, 18 December 2001

> *services for the design, fabrication, engineering and manufacture of the materials and equipment under Japanese Yen Portion I were made and completed in Japan.* ***These services were rendered outside the taxing jurisdiction of the Philippines and are therefore not subject to contractor's tax."*** (Emphasis and underscoring supplied)

Such being the case and since the subject services are rendered by GmbH outside the Philippines, the service fees to be paid therefor by SPI to GmbH are exempt from income tax and consequently from withholding tax. ***(BIR Ruling 068-2013 dated February 18, 2013)***

With respect to VAT, payments for the sale or exchange of services, including the use or lease of properties are subject to VAT only if the services are performed in the Philippines. Section 108 (A) of the National Internal Revenue Code of 1997, as amended, provides that:

> *"SEC. 108. Value-added Tax on Sale of Services and Use or Lease of Properties. -*
>
> *(A) Rate and Base of Tax. - There shall be levied, assessed and collected, a value-added tax equivalent to ten percent (10%) of gross receipts derived from the sale or exchange of services, including the use or lease of properties: Provided, that the President, upon the recommendation of the Secretary of Finance, shall, effective January 1, 2006[2], raise the rate of value-added tax to twelve percent (12%). . .*
>
> *The phrase 'sale or exchange of services' means the performance of all kinds of* ***services in the Philippines*** *for others for a fee, remuneration or consideration. . . "* (Emphasis and underscoring supplied)

Accordingly, since the services are performed by GmbH outside the Philippines, the service fees to be paid therefor by GmbH are likewise exempt from VAT. ***(BIR Ruling 068-2013 dated February 18, 2013)***

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

Very truly yours,

CAESAR R. DULAY
Commissioner of Internal Revenue

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[2] The VAT rate was increased to 12 percent beginning February 1, 2006, in accordance with the Memorandum of the Executive Secretary to the Secretary of Finance dated January 31, 2006, as circularized by Revenue Memorandum Circular No. 7-2006 (Publishing the Full Text of the Memorandum from Executive Secretary Eduardo R. Ermita dated January 31, 2006. Approving the Recommendation of the Secretary of Finance to Increase the Value Added Tax Rate from Ten Percent to Twelve Percent) dated January 31, 2006.