REPUBLIC OF THE PHILIPPINES
DEPARTMENT OF FINANCE
**BUREAU OF INTERNAL REVENUE**

**Quezon City**

| Sections 105 & 108(B)(2) |
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| BIR Ruling No. 119-14<br>BIR Ruling No. 455-2011 |
| #239-2016 |
| 6-6-2016 |

**SAN AUGUSTIN SERVICES INC.**
5th Floor, Pryce Tower, Pryce Business Park
J.P. Laurel Avenue, Davao City

Attention: **Mr. Thomas Charles Henderson**
Director

Gentlemen:

This refers to your letter dated December 9, 2011 requesting for confirmation of your opinion that the onshore services rendered by SAN AUGUSTIN SERVICES INC. ("SASI" for brevity) in favor of MDC America, Inc. ("MDCA" for brevity), a non-resident foreign company not engaged in business in the Philippines, are subject to zero percent (0%) value-added tax (VAT) pursuant to Section 108 (B) (2) of the Tax Code of 1997, as amended.

It is represented that SASI (TIN is a corporation duly organized and existing under Philippine laws, with Securities and Exchange Commission (SEC) Company Registration No. dated June 16, 2011. It is registered with the Bureau of Internal Revenue on June 29, 2011 as VAT registered taxpayer with TIN Its principal place of business is at 5th Floor, Pryce Tower, J.P. Laurel Avenue, Barangay 19-B, Davao City.

SASI is primarily organized to *"render exploration and other mining-related services to persons engaged in the exploration, development and commercial utilization of mineral resources; to provide technical, management, administrative and other services to (1) mining companies or other persons engaged in mining; (2) persons engaged in the acquisition, conveyance, storage, marketing, processing, refining and distribution of minerals; provided, however, that the corporation shall not engage in mining activities for itself but will only render services for its clients"*.

On the other hand, MDCA is a corporation organized and existing under the laws of the State of Washington, United States of America, with registered address at 422 W. Riverside Avenue, Suite 1100, Spokane, Washington, 99201.

On June 28, 2011, a Services Agreement (the "Agreement") was executed by and between MDCA and SASI. Pursuant to the Agreement, MDCA engaged the services of SASI as its onshore service provider to perform the following:

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1. Attend to the procurement and management of suppliers, including the following:

(i) Coordination and liaison with regard to the invitation, assessment, selection and engagement of suppliers;
(ii) Processing of supplier purchase orders and invoices and making the relevant payments;
(iii) Development of long lead time equipment order schedule with an aim to minimize the Project Schedule and taking into account the timing of the Bankable Feasibility Study (BFS) and the Declaration of Mining Project Feasibility (DMPF);
(iv) Development of purchase order documentation and negotiate terms of purchase with long lead tie vendors in connection with the Completion of the BFS and DMPF; and
(v) Development of bid package(s) for selection of contractors and undertake the selection, appointment and management of such contractors in connection with the Completion of the BFS and DMPF;

2. Secure, engage and coordinate qualified personnel required or desirable for the Completion of the BFS and DMPF;

3. Manage the completion and fulfilment of the Exploration Work Program and the Environmental Work Program; and

4. Any other lawful and related services which MDCA requests SASI to perform.

Furthermore, pursuant to the Agreement MDCA shall pay Service Fees to SASI in an amount denominated in the US dollar currency, equivalent to 105% of the actual labor costs incurred by SASI, in pursuance to their Agreement. Payments to be made by MDCA shall be coursed through SASI's nominated dollar bank account.

In reply, please be informed that under Section 105 of the 1997 Tax Code, as amended, it is provided that any person who, in the course of trade or business, sells, barters, exchanges, leases goods or properties, renders services, and any person who imports goods shall be subject to the value-added tax (VAT) imposed in Sections 106 to 108 of the same Code. The phrase 'in the course of trade or business' means the regular conduct or pursuit of a commercial or an economic activity, including transactions incidental thereto, by any person regardless of whether or not the person engaged therein is a non-stock, non-profit private organization (irrespective of the disposition of its net income and whether or not it sells exclusively to members or their guests), or government entity.

Relative to the above provision, Section 108(A) of the 1997 Tax Code, as amended, in providing the test for the applicability of VAT on sale of services, clarifies that 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. The said Section provides, viz.:

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

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> (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, raise the rate of value-added tax to twelve percent (12%). . .
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> 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. . ."

Applying the above provisions in the instant case, it is clear that the payments for the onshore services performed by SASI in favor of its non-resident client, MDCA, which services were performed in the Philippines, are subject to VAT. As regards the VAT rate imposed on the subject services, Section 4.108-5 of Revenue Regulations No. (RR) 16-05, as amended by RR No. 4-2007, implementing Section 108 (B) of the 1997 Tax Code, as amended, provides for the transactions which are subject to the 0% VAT, to wit:

> "SEC. 4.108-5. Zero-Rated Sale of Services. —
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> (a) In general. — A zero-rated sale of service (by a VAT-registered person) is a taxable transaction for VAT purposes, but shall not result in any output tax. However, the input tax on purchases of goods, properties or services related to such zero-rated sale shall be available as tax credit or refund in accordance with these Regulations.
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> (b) Transactions Subject to Zero Percent (0%) VAT Rate. — The following services performed in the Philippines by a VAT-registered person shall be subject to zero percent (0%) VAT rate:
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> (2) Services other than processing, manufacturing or repacking rendered to a person engaged in business conducted outside the Philippines or to a non-resident person not engaged in business who is outside the Philippines when the services are performed, the consideration for which is paid for in acceptable foreign currency and accounted for in accordance with the rules and regulations of the BSP;
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In the case of *CIR vs. Burmeister and Wain Scandinavian Contractor Mindanao, Inc. G.R. No. 153205, Jan. 22, 2007*, the Supreme Court emphasized that certain requisites must be complied with in order that the services may qualify for VAT zero-rating under Section 102 (b) (2) [now Section 108 (B) (2)], viz.:

1. The services must be performed in the Philippines;
2. The services must be rendered to persons engaged in business conducted outside the Philippines or to non-resident persons not engaged in business who are outside the Philippines when the services are performed; and

3. The fees to be paid are in acceptable foreign currency and accounted for in accordance with the rules and regulations of the BSP.

In relation thereto, Section 3(d) of Republic Act (RA) No. 7042 dated June 13, 1991, defines the phrase "doing business", to wit:

"**Section 3.** ***Definitions.*** - As used in this Act:

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d) The phrase "doing business" shall include soliciting orders, service contracts, opening offices, whether called "liaison" offices or branches; appointing representatives or distributors domiciled in the Philippines or who in any calendar year stay in the country for a period or periods totalling one hundred eighty (180) days or more; participating in the management, supervision or control of any domestic business, firm, entity or corporation in the Philippines; and any other act or acts that imply a continuity of commercial dealings or arrangements, and contemplate 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 of the purpose and object of the business organization: Provided, however. That the phrase "doing business: shall not be deemed to include mere investment as a shareholder by a foreign entity in domestic corporations duly registered to do business, and/or the exercise of rights as such investor; nor having a nominee director or officer to represent its interests in such corporation; nor appointing a representative or distributor domiciled in the Philippines which transacts business in its own name and for its own account;"

Furthermore, the terms "doing" or "engaging in" or "transacting" business" were explained in the case of *Mentholatum Co., Inc. et. al. v. Mangaliman, et. al. (072 Phil. 524, G.R. No. 47701 dated June 27, 1941)* where the Supreme Court ruled that:

"No general rule or governing principle can be laid down as to what constitutes "doing" or "engaging in" or "transacting" business. Indeed, each case must be judged in the light of its peculiar environmental circumstances. The true test, however, seems to be whether the foreign corporation is continuing the body or substance of the business or enterprise for which it was organized or whether it has substantially retired from it and turned it over to another. (Traction Cos. v. Collectors of Int. Revenue [C. C. A. Ohio], 223 F. 984, 987.) 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, the purpose and object of its organization.] (Griffin v. Implement Dealers'

Mut. Fire Ins. Co., 241 N. W. 75, 77; Pauline Oil & Gas Co. v. Mutual Tank Line Co., 246 p. 851, 852, 118 Okl. 111; Automotive Material Co. v. American Standard Metal Products Corp., 158 N. E. 698, 703, 327, Ill. 367.)"

In the present case, however, the MDCA cannot be considered as doing business in the Philippines by mere engaging the services of SASI. The duration of the services agreement is not to be construed as engaging in business since the provider of service is SASI and not MDCA. Thus, there is no continuity of commercial dealings on the part of MDCA when it entered into a service agreement with SASI.

Accordingly, since the onshore services are rendered by SASI in favor of MDCA, a non-resident foreign company, not engaged in business in the Philippines, as evidenced by the Certification of Non-Registration of Company issued by SEC dated February 5, 2015, and paid for in acceptable foreign currency, the service fees paid therefor by MDCA is subject to zero percent (0%) VAT pursuant to the above-cited laws and regulations. It must be emphasized, however, that the application of the 0% VAT rate on the sale of services of SASI is not automatic and does not cover all its transactions as it must still show that said transactions fully comply with the above-mentioned requirements. *(BIR Ruling No. 455-2011 dated November 16, 2011)*

Furthermore, it is noted that SASI is neither registered with the Board of Investments (BOI) nor with the Philippine Economic Zone Authority (PEZA). As such, it is subject to the regular income tax rate of thirty percent (30%) on its income derived from export sales. *(BIR Ruling No. 119-2014 dated May 6, 2014)*

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 as null and void.

Very truly yours,

**KIM S. JACINTO-HENARES**
Commissioner of Internal Revenue

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