

REPUBLIC OF THE PHILIPPINES

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SESSION NO. 68

Tuesday, March 8, 2005

**THIRTEENTH CONGRESS
FIRST REGULAR SESSION**

SESSION NO. 68
Tuesday, March 8, 2005

CALL TO ORDER

At 3:47 p.m., the Senate President, Hon. Franklin M. Drilon, called the session to order.

PRAYER

Sen. Mar Roxas led the prayer, to wit:

Dear Lord, we humbly come before You today in prayer, thankful for the many blessings You continue to bestow upon us, and heartily sorry for the numerous times we have not listened to You or have chosen to ignore You.

We pray You continue to shower Your blessings upon us and our entire nation as we go through many challenges towards a brighter and more prosperous tomorrow.

Amen.

ROLL CALL

Upon direction of the Chair, the Secretary of the Senate, Oscar G. Yabes, called the roll, to which the following senators responded:

Angara, E. J.	Lapid, M. L. M.*
Arroyo, J. P.	Magsaysay Jr., R. B.
Cayetano, C. P. S.	Osmeña III, S. R.
Drilon, F. M.	Pangilinan, F. N.
Ejercito Estrada, J.	Pimentel Jr., A. Q.
Ejercito Estrada, L. L. P.	Recto, R. G.
Flavier, J. M.	Revilla Jr., R. B.
Gordon, R. J.	Roxas, M.

With 16 senators present, the Chair declared the presence of a quorum.

Senators Biazon, Madrigal and Villar arrived after the roll call.

Senators Enrile, Lacson and Lim, who were on official mission, also arrived after the roll call.**

Senator Defensor Santiago was on official mission.

* as corrected by Senator Lapid on March 9, 2005

** as corrected by Senator Pangilinan on March 9, 2005

**APPROVAL OF THE JOURNAL
AS CORRECTED**

Upon motion of Senator Pangilinan, there being no objection, the Body dispensed with the reading of the Journal of Session No. 67 and considered it approved subject to the corrections made by Senator Arroyo on page 730, left column, third paragraph, after the word "where" to insert the phrase IF HE FIRES THE CHIEF OF STAFF; and, right column, first sentence, to delete the words "a member" and insert the words HALF A DOZEN MEMBERS WHO.

**ACKNOWLEDGEMENT
OF THE PRESENCE OF GUESTS**

At this juncture, Senator Pangilinan acknowledged the presence of Mayor Ofelia Tria and members of the Sangguniang Bayan of Abuyog, Leyte; Mayor Ed Flores of Minalin, Pampanga; and councilors from Jagna, Bohol.

REFERENCE OF BUSINESS

The Secretary of the Senate read the following matters and the Chair made the corresponding referrals:

**MESSAGES OF THE PRESIDENT
OF THE PHILIPPINES**

Letters of Her Excellency, President Gloria Macapagal Arroyo, dated February 24 and March 1, 2005, respectively, submitting to the Senate for its consideration and concurrence the following:

Agreement Establishing the Advisory Centre on WTO Law, signed in Seattle, Washington, USA on 1 December 1999; and

United Nations Convention Corruption, signed by the Philippines on 9 December 2003

To the Committee on Foreign Relations

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BILL ON FIRST READING

Senate Bill No. 1951, entitled

AN ACT INSTITUTIONALIZING REFORMS IN REAL PROPERTY APPRAISAL AND ASSESSMENT PRACTICES IN THE PHILIPPINES, CREATING FOR THE PURPOSE THE NATIONAL APPRAISAL AUTHORITY AND FOR OTHER PURPOSES

Introduced by Senator Angara

To the Committees on Ways and Means; Local Government; and Finance

RESOLUTIONS

Proposed Senate Resolution No. 204, entitled

RESOLUTION URGING THE COMMITTEE ON LABOR AND EMPLOYMENT TO CONDUCT AN INQUIRY, IN AID OF LEGISLATION, ON THE IMPACT ON THE ECONOMY, PARTICULARLY ON LABOR AND EMPLOYMENT AND ON THE WELFARE AND INTEREST OF OVERSEAS FILIPINO WORKERS IN AND BOUND FOR JAPAN, OF THE CHANGE IN THE IMMIGRATION RULES OF JAPAN REGARDING THE ENTRY OF OVERSEAS PERFORMING ARTISTS, OR OPAS, ON THE CAUSES OF SUCH CHANGE, AND THE RESPONSE OF THE DEPARTMENT OF LABOR AND EMPLOYMENT, PHILIPPINE OVERSEAS EMPLOYMENT ADMINISTRATION, AND THE DEPARTMENT OF FOREIGN AFFAIRS ON THE SAME

Introduced by Senator Ramon "Bong" Revilla Jr.

To the Committees on Foreign Relations; and Labor, Employment and Human Resources Development

Proposed Senate Resolution No. 205, entitled

RESOLUTION DIRECTING THE COMMITTEE ON NATIONAL

DEFENSE AND SECURITY TO CONDUCT AN INQUIRY, IN AID OF LEGISLATION, ON THE REPORTED ANOMALOUS PURCHASE BY THE ARMED FORCES OF THE PHILIPPINES OF 1,700 UNITS OF M249 SQUAD AUTOMATIC WEAPON, OR MINIMI'S WORTH P593.3 MILLION PARTICULARLY ON THE ALLEGED OVERPRICING THEREOF

Introduced by Senator Biazon

To the Committees on National Defense and Security; and Accountability of Public Officers and Investigations

COMMUNICATION

Letter from Executive Secretary Eduardo R. Ermita of the Office of the President of the Philippines, transmitting to the Senate the letter of Her Excellency President Gloria Macapagal Arroyo addressed to Speaker Jose C. De Venecia Jr. of the House of Representatives, certifying to the necessity of the immediate enactment of House Bill No. 3740, entitled

AN ACT TO EXTEND THE UTILIZATION PERIOD OF THE AGRICULTURAL COMPETITIVENESS ENHANCEMENT FUND, AMENDING SECTION 8 OF THE REPUBLIC ACT NO. 8178, ENTITLED AN ACT REPLACING QUANTITATIVE IMPORT RESTRICTION ON AGRICULTURAL PRODUCTS, EXCEPT RICE, WITH TARIFFS, CREATING THE AGRICULTURAL COMPETITIVENESS ENHANCEMENT FUND, AND FOR OTHER PURPOSES,

pursuant to the provisions of Article VI, Section 26(2) of the Constitution.

To the Committee on Rules

PARLIAMENTARY INQUIRY OF SENATOR PIMENTEL

Senator Pimentel stated that House Bill No. 3356, extending the effectivity of the Rent

Control Law, was approved by the House of Representatives and transmitted to the Senate as early as January 17, 2005, but to date there seems to be no action on it on the committee level. He inquired on the status of the bill in the light of a similar measure that Senator Recto filed in September 2004.

Senator Pangilinan clarified that contrary to the claim that nothing has been done about the bill, the Committee on Urban Planning, Housing and Resettlement has already conducted hearings on it.

As committee chair, Senator Biazon informed the Body that House Bill No. 3356 was approved by the House in the first week of January during the special session but at that time, he said, the Rent Control Law had already expired. He disclosed that in a discussion with some congressmen, and in consultation with the stakeholders and the concerned government agencies, it was agreed that it would be better to reenact the law for which reason, another committee report based on the Recto bill would be submitted for the Body's consideration within the week.

Senator Pimentel thanked Senator Biazon for giving that assurance as he expressed hope that the bill would be enacted before the end of the year.

SUSPENSION OF SESSION

Upon motion of Senator Pangilinan, the session was suspended.

It was 4:02 p.m.

RESUMPTION OF SESSION

At 4:04 p.m., the session was resumed.

COMMITTEE REPORT NO. 16 ON SENATE BILL NO. 1950

(Continuation)

Upon motion of Senator Pangilinan, there being no objection, the Body resumed consideration, on Second Reading, of Senate Bill No. 1950 (Committee Report No. 16), entitled

AN ACT AMENDING SECTIONS 27, 28,
34, 106, 108, 109, 110, 111, 112, 113,
116, 117, 118, 119, 125, 148, 236, 237,
AND 288 OF THE NATIONAL

INTERNAL REVENUE CODE OF 1997, AS AMENDED, AND FOR OTHER PURPOSES.

Senator Pangilinan stated that the parliamentary status was the period of interpellations.

Thereupon, the Chair recognized Senator Recto, Sponsor of the measure, and Senator Osmeña for his interpellation.

INTERPELLATION OF SENATOR OSMEÑA

At the outset, Senator Osmeña congratulated Senator Recto for drafting the committee report and for anticipating that it would not be an easy task to obtain the Body's approval of the VAT measure. He stated that tax measures are controversial because they hurt some or all people, especially those who cannot afford to pay. He pointed out that it is the responsibility of the senators to know what the proposed measure is all about because if one does not fully understand it, then one cannot vote for or against it. He stressed that the measure affects the entire Filipino people and they should be properly informed of the effects once the bill is passed into law. He informed the Body that he would like to put on record the meaning of each and every provision of the measure because a lot of legislations were passed that were not properly explained and later on questioned in the courts which, in turn, could not even interpret the legislative intent.

Adverting to the part of the sponsorship speech where Senator Recto mentioned that by the time he finished the speech, the government would have borrowed more than P21 million, Senator Osmeña asked if it was on a per hour basis. Senator Recto calculated it to be P1,060,000 per minute assuming the speech was roughly about 20 minutes.

Asked why the country is in such a situation, Senator Recto attributed it to the large deficit, government spending more than what it earned and, therefore, borrowing more money to finance the gap.

Senator Osmeña observed that the country has gone through several cycles where there is always a budget deficit and a surplus at one time. Upon query, Senator Recto affirmed that the government has been living beyond its means. He opined that if the growth of the economy is faster than the growth of debt, the debts would all be paid.

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Senator Osmeña stated that the volume of debt increased in the last four years and the administration's borrowings contributed to the consolidated public sector debt amounting to over P1 trillion. Senator Recto agreed.

Asked if the total consolidated public sector during the Estrada administration was between P300 million to P400 million only, Senator Recto replied that he does not have the exact figure. Senator Osmeña requested that the exact figure be provided. Senator Recto said that he would request the finance officials to furnish the data.

Asked why the present generation is being blamed in the speech for the current debt, Senator Recto replied that most of the debts were accumulated by the present generation. He clarified that he was referring to the generation of leaders, including himself. He affirmed that the word "generation" refers to the generation of leaders.

Senator Osmeña asked to be clarified how it could be the fault of this generation's leaders when all the debts were accumulated by institutions like Napocor, GSIS, SSS and NFA. Senator Recto explained that the budget of the national government is approved by Congress and there were many instances when the Body voted consciously in favor of the budget with its corresponding deficits.

But Senator Osmeña pointed out that the Body has always objected to the GOCCs contribution to the consolidated public sector debt and examined why it ballooned to such a huge amount. He stressed that the Body has always questioned why the GOCCs were able to borrow without the approval of Congress and all unpaid dues were shouldered by the government. Senator Recto cited the case of EPIRA where the national government assumed the P200 billion debt of Napocor.

Senator Osmeña informed the Body that it is mandated in the EPIRA that the national government or the Napocor cannot pass the P200 billion debt burden to the consumers by increasing the power charges. He added that at present, Napocor owes \$10 billion and selling all its assets would only raise a maximum amount of \$5 billion. The stranded financial debt is about \$5 billion and the government would have to pay said amount, he noted. A "stranded cost," he explained, is the unused portion of the money allotted to pay the IPPs

that amounts to about \$10 billion which cannot be collected at present given Napocor's current market rates. He pointed out that the failure of this generation's leaders is that they have not watched the debt pile up because the debt was not presented clearly, and that it continues to increase.

Asked if the bill provides that the GOCCs are prohibited from entering into loans without the approval of Congress and the national government is not allowed to automatically guarantee all the loans entered into by the GOCCs, Senator Recto replied that matters concerning the GOCCs are not part of the bill. He stated that he has yet to confirm if there are bills on said issues.

Relative thereto, Senator Osmeña stated that the Filipino people should be assured that the same problem would not recur. He pointed out that if the bill is to be approved without that safety measure, it would be easy for institutions to continue borrowing and pass the burden of paying to the national government in case they could not afford. Senator Recto pointed out that the Napocor issue would be properly dealt with by the ERC, as the measure cannot solve all the deficit problems.

Senator Recto remarked that the present generation is responsible for the debt and as parents, it is the obligation of the legislators to clean up the mess so as not to pass the burden to the children.

Senator Osmeña asserted that every Filipino is considered the child of all the 23 senators, and it is the responsibility of the senators to look after the welfare of the child. He stated that Congress was given the power to raise taxes and it has the duty to make sure that taxes are not raised unless for very good reasons. He observed that everyone suffers because of the consolidated public sector debt and increased taxes are being proposed to put the fiscal position of the country in a better shape. He pointed out that before imposing new taxes, there should be an assurance that all loopholes are plugged. He said that the biggest concern is the debts incurred by the GOCCs and the Filipino people should be given the assurance that whatever money is raised from the increased taxes would not go to the payment of additional debts.

On the related matter, Senator Osmeña lamented that in the North Railway project, the government incurred an additional \$500 million loan

that did not pass through Congress. He added that with the bill, legislators would be giving the administration a blank check since funds could be raised through the VAT. Moreover, he surmised that government would only plug the fiscal deficit but not the loopholes because the GOCCs could continue to borrow without the approval of Congress.

Agreeing to the observation, Senator Recto said he, in fact, supported the initiative to look into the North Railway project. He stressed that plugging the loophole in the VAT is his concern for which reason, the bill is recommending the lifting of the VAT exemptions of the power and petroleum industries that are first in the VAT chain, as he added that the VAT system would not work if the upstream industries are not included.

Senator Osmeña noted that there has been no commitment from Congress or the national government to plug the loopholes on the GOCCs. He expressed hope that such commitment would be made for the sake of the people. Additionally, he noted that smuggling and tax evasion are loopholes and even the proposed VAT increase is an administrative loophole since it is already being paid by the purchasers of goods that are manufactured locally. Senator Recto disagreed as he noted that technically, these manufactured goods are VAT exempt. However, Senator Osmeña argued that while officially no taxes are collected on the power industry level, VAT is being collected from consumers since the price of any item they purchase, aside from the VAT paid on the total amount, also includes the cost of power.

Senator Recto conceded that VAT is being paid on consumer purchases; however, he said that it is difficult to say that people are paying VAT on power as the power cost is already part of the purchase price. Further, he said that technically people are not paying VAT on power since there is no VAT on the power industry.

Senator Osmeña pointed out that even officials of the Departments of Finance and Energy acknowledged that should the government start collecting VAT on the power industry, the net tax take would not be that big since VAT is already effectively being paid on power by the commercial users. He stated that the residential user stands to suffer the most since he has no customer to which he can pass on the VAT.

In terms of applied economics, Senator Recto disagreed with the argument as he noted that it was premised on a perfect VAT system wherein prices would not go up with the imposition of this additional tax. Additionally, he believed that although theoretically, prices should not increase as a result of the VAT, past experience has proven otherwise. Even today, he noted that media reports have shown that the sellers have already increased prices in anticipation of the VAT.

For his part, Senator Osmeña believed that merchants use the impending passage of the VAT measure to justify a price increase even though in truth and in fact, there is no justification for it. As such, he said, the business judgment of these entrepreneurs cannot be questioned since most of them belong to unregulated sectors or subsectors.

Senator Recto argued that the same principle would apply, for instance, to the North Expressway wherein the 400% toll rate hike and improvement of roads are supposed to help motorists save money; however, the prices of goods and services still went up. Additionally, he said that he had a problem with theoretical economies since in most instances, the reality is different. Senator Osmeña said that he is not a theoretical economist although both he and Senator Recto had studied the same materials on VAT.

Senator Osmeña also pointed out that many senators did not attend the committee hearings on the measure nor read the transcripts of the hearings.

Senator Osmeña wondered how many people the BIR and the Bureau of Customs have sent to jail for tax fraud or smuggling in the last 5, 10 or 15 years considering that corruption in the revenue-collecting agencies is also one of the biggest financial loopholes. Senator Recto said that he would ask the Department of Finance to provide Senator Osmeña the data so that it could be spread on the record.

Senator Osmeña recalled that the answer to the same query during the public hearing was that the BIR and the Bureau of Customs have not sent anyone to jail nor have any of their own personnel been jailed for anomalies. Further, he noted that in developed economies, laws are respected simply because there is a certainty of punishment; for instance, Americans pay their income taxes because

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they know that the Internal Revenue Service (IRS) would go after them if they do not. Moreover, he noted that the infamous mobster Al Capone was jailed for tax fraud, not for murder, moonshining or gunrunning. He opined that unless there is political will to enforce laws, the government would just continue to raise taxes even as it allows tax evaders to go scot-free. He added that this commitment, aside from the earlier commitment to plug the loopholes on GOCC borrowings, is what he would like to get from the current and future administrations. Senator Recto expressed hope that the Executive department would be able to do the same.

Senator Osmeña stressed that he wanted to justify the proposed VAT hike to constituents who would be affected by the measure and to tell them that he was able to get a commitment from the administration that all loopholes would be plugged even if it means sending tax evaders to jail. Unless this is done, he said that he might as well vote against the measure as he asserted that it is unjust and unfair to continue expanding the taxes without making the proper moves to plug the loopholes. Senator Recto gave assurance that the Executive department is doing its best to act on these concerns.

Senator Osmeña recalled a news report that the Deputy Collector of Customs was refused entry into the Cebu City Customs bureau by the local customs director. He wondered why political will is not being exercised when the government is supposed to begin removing corrupt officials in the revenue collecting agencies. Senator Recto said that the Presidential Legislative Liaison Officer as well as the officials from the Department of Finance were present and taking notes of the discussion. Senator Osmeña, however, said that it is not these people but elected officials such as the senators who answer to the people. He pointed out that the Senate could not simply pass any bill proposed by Malacañang as it had done in the case of the Sin Tax Law or the Lateral Attrition Law without any commitment for the Executive that it would plug the loopholes. He said that the P81 billion collectible in taxes through the proposed VAT increase is more than 10% of the total revenue take of the government. He also noted that the government is collecting P700 billion to which Congress would now add another P80 billion on top of the P30 billion that is expected to be collected from the Lateral Attrition Law and Sin Tax Law.

Senator Recto clarified that the sin taxes would generate P15 billion while the Lateral Attrition Law would bring in about P10 billion. Further, he said that only about P64 billion would be generated since P17.5 billion would be given away.

Adverting to the speech, Senator Osmeña wondered how the Lateral Attrition Law would make honest men out of tax men. Senator Recto replied that incentives were provided for all personnel of the agency. Further, he said that if the local revenue office hits its target even if the national government does not, the local agency still receives the incentive; on the other hand, agency personnel could be fired if they miss the target by 7.5%.

Senator Osmeña said that he had tried his best to cooperate with the administration by voting for the Lateral Attrition Law. Senator Recto maintained that the committee report, in effect, also sided with the Opposition because VAT would not be increased from 10% to 12%. Senator Osmeña agreed, saying that otherwise, he would not have signed the report.

Senator Osmeña noted that the Committee held nine public hearings which lasted for 30 hours and were attended by more than 1,000 people. He expressed concern that only a few senators have a working understanding of the measure at this point. He asked how many senators attended the hearings. Senator Recto shared the same view as he disclosed that only the following senators attended the committee hearings: Senators Osmeña, Arroyo, Enrile, Flavio, Ejercito Estrada (J), Villar, Biazon, Roxas and Gordon.

Senator Osmeña warned against misleading the public that the Senate had a complete hearing and the senators have a good understanding of the measure because in spite of his effort to do his homework, he still does not understand the bill which is quite complex. Senator Recto assured the Body that he has a fair understanding of the measure and can defend every provision therein.

Upon queries, Senator Recto informed the Body that VAT is an indirect tax, a consumption tax, and generally, a regressive tax.

Adverting to the statement that a tax system which allows the most profitable companies in the country like the Mirant coal-fired power plant not to

pay VAT while a small store beside it is made to pay VAT fails the fairness test, Senator Osmeña wondered whether Mirant would shoulder the VAT or pass it on to the consumers. Senator Recto replied that the liability is with the seller of the product or service, not with the consumer. He said that if the seller does not pay 10% tax on its gross sales, he would have to justify it by showing to the BIR his receipts of purchases to recover the input VAT; whereas, a small store with gross sales of P550,000, for example, has the administrative burden of collecting from the consumer the required tax because it is liable to pay 10% on its gross sales to the BIR; anything less than that would necessitate the presentation of the corresponding receipts and pertinent documents to the BIR. On the other hand, he said, a power or a petroleum company does not have the same burden and cannot be audited by the BIR for its purchases. He noted that the reason there is a vast leakage in the VAT amounting to as high as P240 billion is that large industries are exempt from VAT, hence, destroying the entire VAT chain. Like small stores and mom and pop operators, he believed that these large companies should be made to pay VAT.

On whether Mirant would be made to pay VAT, Senator Recto replied that it would pass on the tax to the consumers.

Senator Osmeña opined that the seller, in other words, would only be a collector of tax because he would only pass it on to the consumer. Senator Recto agreed as he clarified that the process would allow the BIR to audit the entire VAT chain.

Senator Osmeña said that he is convinced about the administrative efficiency and elegance of the VAT system. He agreed that if there are no intermediate producers that are VAT-exempt, the administrative headache of the BIR is lessened considerably. He asserted that this would be lessened further if there is a single rate instead of a two-tier VAT rate.

Senator Recto cited the case of the telecom industry which has three major players, one of which gives a lower rate with its promotional package of 24/7. He said that while this particular player collects some VAT from consumers, it shoulders some of the costs. He said that it depends on the pricing power of the industry but in this case, the company may pass it on to consumers but

shoulder some of the burden because not all the industries that would be imposed a VAT would do the same. However, he clarified that in the case of power industry, Mirant, for instance, there is a fixed contract that allows the company to pass on the tax, that is why there is no "pass-on provision" in the bill.

Senator Osmeña acknowledged the reality that all businessmen would try to pass on all costs to the consumers. Relative thereto, he read the dispositive portion of the original contract between Mirant, which was originally known as Hopewell Energy International Ltd., with the government, to wit:

Napocor shall be responsible for payment of all taxes, import duties, fees, charges, and other levies imposed by the national government of the Republic of the Philippines, or any agency or instrumentality thereof to which Hopewell Philippines may, at any time, be or become subject in or in relation to the performance of their obligations under this agreement other than:

1. Taxes imposed or calculated on the basis of net income of Hopewell Philippines; and
2. Construction permit fees, environmental permit fees, and other similar fees and charges; and all real estate taxes, assessment rates, and other charges in respect of the site, buildings, improvements thereon.

In other words, Senator Osmeña said, the company would pay real estate tax and income taxes to the local government; however, he noted the company's huge tax credits because of its original tax-free importation of capital equipment and other capital expenditures.

Upon further queries, Senator Recto informed the Body that an additional P12.5 billion would be collected this year.

Referring to the speech, Senator Osmeña wondered how many Filipinos are able to enjoy a breakfast that has rice, *galunggong*, *kamatis*, *bagoong*, egg, *kapeng barako* with *muscovado* while reading the *dyario*. He adverted to some reports that in many areas of the country, even kids put salt on their rice for lack of a viand.

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Asked how much power rate increase a laborer would shoulder if he only consumes 200 kilowatts per month, Senator Recto replied that there is a lifeline subsidy if the laborer consumes less than that or 100 kilowatts; but just the same, the rate would go up. But he observed that most of the poor, and even the middle class, consume more petroleum than power.

Senator Osmeña stated that a 200-kilowatt consumption is like a *bahay-kubo* type consumption. He disclosed that it is only Meralco and one or two other distributors that enforce the lifeline rate; the cooperatives do not, hence, everybody has to bear the full cost of power even if the poor consume less than 100 kilowatts a month. He stated that right after the elections last year, Napocor was able to obtain from the ERC the equivalent of two-rate increases with a total amount of about P1.30 to P1.40 per kilowatt-hour. He said that Napocor has a pending rate increase of about P1.30 per kilowatt-hour which might be approved any time, hence, it would be another P260 for a 200-kilowatt consumption. As regards the oil price, he said that it was \$54 a barrel as of yesterday.

On the reduction of the excise tax on socially sensitive products such as diesel, bunker fuel and kerosene, Senator Recto stated that under the bill, kerosene would be reduced from P.60 to 0; diesel from P1.63 to 0; bunker fuel from P.30 to 0. He said that the pump price of diesel as of February 26 was P24.21.

Thereafter, Senator Osmeña inquired about the net increase of the diesel price under the bill.

SUSPENSION OF SESSION

Upon motion of Senator Osmeña, the session was suspended.

It was 5:08 p.m.

RESUMPTION OF SESSION

At 5:08 p.m., the session was resumed.

Senator Recto explained that under the bill, the present pump price of diesel of P24.21 would be reduced by P1.63 to P22.58, after which a 10% VAT or P2.26 would be added, bringing the price to P24.84 or an increase of P.63. He said that the Executive wanted the diesel price to go up by P2.91 to P27.12 per liter, a move that would hit the riding

public hard and would be inflationary. He added that the calculated cost per passenger is an additional P.25.

As for the LPG, Senator Recto stated that it enjoys a present excise tax of zero. He said that under the bill, it would be increased by 10% as against the Executive's 12%.

On kerosene, Senator Recto said that while the retail price is P24.81 per liter, it would be reduced by P.60 and an additional 10% VAT would give it a net gain of P1.82, while under the DoF proposal, it would be P2.98.

Senator Osmeña observed that while the DoF wants a blank check, it is up to the Senate and the House to keep them in check. He said that if the DoF were left alone, it would just balance the budget and it would be up to Congress to determine who gets hurt.

On the matter of the P750,000 threshold income, Senator Recto stated that the P750,000 is a conservative amount since the threshold was P550,000 when the law was passed in 1996. He added that if that amount is indexed, it would roughly come out to P750,000. However, he said that the amount is still low since the threshold should be P1.2 million.

Upon query, Senator Recto stated that the base was P550,000 plus CPI, adding that there is no record as to how that amount was arrived at.

On the matter of quantifying the losses of potential income if the threshold is raised to P2 million, Senator Recto said that the BIR and the DoF would provide the Body information on the matter.

Senator Recto pointed out that the reason for a higher threshold is that there is going to be an administrative cost on the part of the taxpayer to be under the VAT. He stated that as far as the BIR is concerned, there is going to be an administrative cost in monitoring a VAT payer. He said that those with P750,000 gross income might not have much value added to begin with.

Senator Osmena pointed out that the magic number is below P750,000 that would automatically exempt the individual from paying VAT.

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Senator Recto further explained that the gross sale should not exceed P750,000 but if the individual expects that the threshold would be exceeded, he has to register.

In a situation where the gross sale last year was P300,000 and it reached P1 million this year, asked if the individual would be sued by the BIR, Senator Recto replied in the negative, as he clarified that if the individual is not registered even if his gross sale hit P1 million, he would not owe government VAT.

Asked if the individual would have to register if his gross sale hit P1 million in one year and surpassed P750,000 the next year, Senator Recto replied in the affirmative. He added that as long as the individual is registered, his gross sale, regardless of the amount, would be subject to VAT. He pointed out that there is a simplified procedure on registration that is found in the committee report.

On whether a registered individual who paid 10% VAT on his P500,000 gross sale in a given year could recover that amount, Senator Recto stated that if the individual has receipts to show his VAT inputs, he pays less than 10%.

Asked if an individual, who paid VAT every month but realized in October that his gross sales would not reach P750,000, could get his VAT payments back in case he decides to deregister, Senator Recto stated that the VAT-registered individual did not lose anything because being in the VAT system, he was able to credit the VAT inputs he paid. He pointed out that the individual could make a comparison between paying 3% on gross sale and being in the VAT system and make a judgment call if he wants to be deregistered or not.

To the observation that it would be a difficult system for an individual who is grossing P50,000 a month, Senator Recto countered that it is still a better system than the existing one, the same system applied in other countries. He argued that there is nothing wrong about being VAT-registered because it is a pass-on tax. He averred that small businessmen are better off under the VAT system than paying 3% on gross sale.

Senator Osmeña asserted that a businessman enjoying a 60% margin is paying VAT on the 60%,

meaning, he is VAT-credited. He stated that the individual, however, would want to get back the VAT payment in case he makes less than P750,000. He anticipated that there would be problems because some people would compare VAT to the income tax where, if the income is low, the individual does not pay any tax.

In response, Senator Recto stated that the threshold is used only for purposes of 1) the administrative burden on the part of the taxpayer; and 2) the administrative burden on the part of the BIR. A problem arises, he said, if gross sale reaches P750,000, or P60,000 a month, in which case the individual hires an accountant, keeps different sets of books, and goes to the BIR to make monthly payments. He stated that it is not a question of fairness in the sense that an individual is making more under the percentage tax or making more under the VAT system. He said that the VAT, being a pass-on tax, does not affect one's gross margin or value added.

Senator Osmeña, however, pointed out that in competitive industries, there would be a pricing problem because a seller could not quote a price separate from the VAT; likewise, a customer would naturally be more concerned about getting better value for his money. Senator Recto replied that precisely, Section 108 of the Code ensures that goods and services should be similarly taxed, but if the good or service is VAT-exempt, then it is VAT-exempt regardless of its cost.

Between two items on which VAT is imposed, for instance, jewelry made from puka shells sold at P1,025 and jewelry made from carabao horn sold at P1,100, Senator Osmeña contended that the seller of puka shell jewelry would opt not to sell his items for more than P1,025 but instead absorb the tax to avoid losing his market.

Noting that laws exempt power companies from administrative hassles, Senator Recto reiterated that there should be no exemptions. He lamented that while doctors and lawyers with income above the threshold would be subject to VAT, big businesses that are actually first in the VAT chain are exempt today, the reason why there are leakages. However, he gave assurance that the sections on the administrative capability of the VAT would be improved. *A*

Senator Osmeña recalled that neither he nor Senator Recto were members of either Houses of Congress which passed the original VAT bill that exempted certain industries, especially fuel, in the belief that prices would be kept lower for the consumer because the product affects everyone. He believed that the legislators had honest intentions when they crafted the law.

Senator Recto explained that he wanted simply to improve the VAT system to lighten the burden of the consumers, not by having multiple rates but by reducing taxes without breaking the VAT system which should work properly if upstream and basic industries that are first in the VAT chain, would be included.

While he agreed that every item in the VAT chain should be subject to VAT, Senator Osmeña believed that the legislators who passed the original VAT bill was very objective in not wanting to cause any more increases in the prices of fuel. Senator Recto said that he was not questioning the intent of the legislators but there were many other ways of doing it without destroying the VAT system.

Replying to a query, Senator Recto affirmed that exporters are exempted from VAT if they are registered and this exemption could also be applied to their income and other taxes, or they could sell their tax credit certificates. He said that the mechanism of a crediting system was established because Congress did not appropriate a budget for refund.

Asked whether this was the reason why the semi-conductor industry was up in arms against the VAT on power, Senator Recto said that the complaints did not make any sense because, as pointed out earlier by Senator Osmeña, government would not collect incremental revenues from an intermediary within a VAT system. Assuming that prices go up and the manufacturers of semi-conductors pay VAT on VAT inputs, he said that they could credit the VAT on their other tax liabilities.

Given the fact that manufacturers could not get a refund from the government, Senator Osmeña believed that VAT would be a cost to them because they have to sell tax credit certificates at a discount, aside from the fact that they shoulder the carrying cost of the original amount paid to the government.

Senator Recto expressed willingness to provide a refund system in the bill.

On the information that VAT is imposed on power in other countries, Senator Osmeña pointed out that power is only P3.50 in Thailand while it is P7 in the Philippines; therefore, increasing it too high would cause further the flight of many investors.

Senator Recto said that power in the Philippines is so expensive because of reliance on imported fuel and other factors like the onerous contracts with IPPs. He believed that power *per se* should not be tax-free considering its true cost. Senator Osmeña argued, however, that for an investor, the cost component is the primary consideration for which reason, he would rather go to a country where power cost is minimal. Senator Recto said that a sophisticated investor would understand that the VAT system is an input-output mechanism.

Senator Osmeña reminded that the candy manufacturers, drug manufacturers, and even Procter and Gamble and Unilever have already left the country, albeit quietly so as not to get the ire of the Filipino consumers. Senator Recto pointed out that these industries left for various reasons such as the peace and order situation, political instability, lack of infrastructure, fiscal deficit, smallness of the market, and judiciary issues, not because of VAT.

As to the statement in the speech that the "provision will cancel the zero VAT-rated privilege of IPPs which some say was sneaked in through the sidedoor of the bicameral conference committee on the EPIRA," Senator Osmeña asked what the phrase "sneaked in through the sidedoor" meant. Senator Recto said that he only heard the statement from Congressman Teves in a TV program on ANC who alleged that the provision was not discussed in the House and in the Senate. He admitted that he did not know whether this was true because he was not a member of the bicameral conference committee on the bill, the reason why he said, "which some say."

Senator Osmeña said that if anybody bothered, he would have asked who attended the bicameral conference. He pointed out that the Supreme Court had already ruled that new sections or new items could be introduced during the bicameral conference as long as both Houses of Congress ratify them. Furthermore, he said that in *Tolentino*

vs. *the Secretary of Finance*, the Supreme Court upheld the power of the Senate to amend *in toto* any bill that was sent to it or is pending in the Bigger House, even if it is an appropriation bill.

Senator Osmeña said that the handful of IPPs that did not have contracts with Napocor asked for a level playing field by either giving them the equivalent of a zero-rated VAT, or taxing the IPPs that have contracts with Napocor, as stated in Napocor's contracts with Casecnan, San Roque, Hopewell I, Hopewell II, Hopewell III, and Pagbilao power plants.

He stated that when the Senate convened for a special session to enact the EPIRA law, he attended 11 of the 13 meetings and this was the reason he took offense to the statement that the matter was sneaked in through the sidedoor. He pointed out that while the IPP contracts with Napocor are zero-rated, the measure is trying to break the zero rating of VAT that might result in the IPPs' filing of a case against the government.

On Senator Recto's statement that VAT can validate and reconcile taxes paid at the point of landing and production, Senator Osmeña asked whether Subic, which has been one of the biggest producers of goods that does not pay taxes, is within customs territory. Senator Recto replied that since Subic is a free port zone, it has a different set of Customs rules; but once the goods are brought out of Subic, these are subject to tax.

Asked how the Customs people keep watch over Subic, particularly the alcohol products that have been coming in which are subject to tax, Senator Recto said that the country might not hit this year's target on excise taxes on sin products. He pointed out that Duty Free Philippines in Manila still imposes the previous year's rate of excise taxes on cigarettes when the new rates should have been applied on January 1, 2005.

Senator Osmeña stated that while government has not plugged the loopholes, the DoF should be warned that the bill would not be passed unless there are improvements in tax collection because it is not fair that smugglers get away scot-free when the rest of the Filipino people are asked to pay higher taxes.

Asked how the DoF would address the point raised by Senator Recto that "the VAT will end the

Only in da Pilipins phenomenon of diesel use going down by 260 million liters a year at a time when 300,000 more diesel-engine cars went on the road, or of national gasoline consumption plummeting by 880 million liters between 1998 and 2003 when the number of gas-fed cars actually jumped by 460,000 units during the same period," Senator Recto said that the VAT system would be much better for the petroleum sector in addressing the problem of oil smuggling. Under the excise tax regime, he pointed out that there is no mechanism for an audit system, so one can smuggle oil and not pay the excise tax. He said that in the computations that the DoF did for the revenues to be generated from this bill, the Committee did not even factor improvements on efficiency with regard to smuggling of petroleum products.

Senator Osmeña agreed, saying that it is harder to smuggle fuel than cigarettes and illegal logs. Senator Recto disclosed that under the bill, non-food agricultural products are subject to VAT, and these include the importation and purchase of logs domestically. However, he said that *copra* is still exempt as it could be used as a food additive.

Asked whether cooperatives are exempt from VAT, Senator Recto stated that since the power sector is subject to VAT, the same applies to electric cooperatives, although he did not support it to be part of the bill. However, he said that agricultural and credit cooperatives should be exempt from VAT.

Pointing out that a cooperative like a corporation, association and partnership is merely a generic term for people coming together for a common activity and enjoy the benefits of economies of scale, Senator Osmeña said that it is difficult not to tax cooperatives because exempting certain cooperatives who produce the same products as those who are not members of a cooperative might result in a two-tiered pricing system that is extortionary. He pointed out that a sugar producer who sells through the cooperative free of VAT could lower his price by 10% and grab the market for the industrial users from the sugar farmer who refines and directly sells sugar that is subject to VAT, thereby promoting an unlevel playing field.

Senator Recto said that to address the particular problem, the Committee increased the presumptive import tax of sugar to 4%.

Senator Osmeña said that he would reserve his right for further interpellation on the measure at a later date.

INTERPELLATION OF SENATOR ENRILE

Asked by Senator Enrile whether the VAT is a transactional tax, Senator Recto replied in the affirmative.

Senator Enrile stated that the VAT is not a tax on production or service but on a transaction – sale, exchange or barter, or letting out of goods, property or services so that an unsold agricultural product is not subject to VAT and neither is the service not rendered by a doctor or lawyer.

On whether the ultimate bearer of the VAT impositions would be the consumers and that the incidence of tax does not really bear on the so called “taxpayer,” Senator Recto replied in the affirmative. But he said it does not necessarily mean that prices should increase all the time.

Asked why stock market transactions are treated differently, Senator Recto replied that it is difficult to impose VAT on financial services of stock transactions.

Pointing out that the stock market is subject to a VAT of 1.5%, Senator Enrile asked why it is being singled out for special treatment when it is the most capable payer of VAT. Senator Recto replied that a stock transaction tax, not VAT, is imposed.

Asked why the stock market should not be taxed like electricity since Congress is looking for sources of revenue for the government, Senator Recto posed no objection to increasing the stock transaction tax but he does not know of any country in a VAT system that imposes VAT on stock transactions.

Senator Enrile opined that there is no reason why the stock transaction tax would not be within the capability and power of Congress to modify and increase. He said that if Congress wants to apply the principle of equity and fairness, and spread the burden among the people, then the burden should reach the players in the stock market. He pointed out that the bill under consideration went beyond the area of VAT towards the corporate field by taxing the income of corporations. Senator Recto agreed

that it is within the taxing power of Congress to increase the stock transaction tax but the Body should look into the pros and cons of whatever rate it would apply.

Senator Enrile wondered why Section 106(A) limits the imposition of VAT to the sale, barter or exchange of goods or property located in the Customs territory of the Philippines at the time of sale. The Subic Freeport like other special economic zones, he pointed out, was created by law to be outside Customs jurisdiction but within Philippine territory, they are covered by the internal revenue laws. He asked whether somebody who is not a locator but puts up a restaurant or hotel in the freeport should be exempt from internal revenue taxes. Senator Recto replied in the negative, saying that he would accept an amendment to the particular provision at the proper time. He stated that VAT should be imposed on goods or services whether these are in Subic or anywhere in the country as long as these goods and services are not exempt transactions.

Senator Enrile stressed that if a locator imports goods into Subic and sells it inside the base, the locator should be subject to internal revenue laws. He cautioned the Body to be careful as the provision might open a very wide area of leakage.

Senator Recto underscored that the bill would not exempt industries in Subic from VAT. In fact, he said, goods for export are zero-rated; a restaurant is subject to VAT and if an export industry uses the facilities of that restaurant, it is subject to VAT. He said that a vehicle that is imported by a locator for use in Subic is not subject to duties, excise tax and VAT, but if the vehicle is used outside Subic, it is subject to duties, excise tax and VAT.

At this point, Senator Enrile suggested that the Secretariat prepare a new copy of the measure to reflect the entirety of the provisions as these are related to the debate. Senator Recto said that the Committee did not touch the provisions not reflected in the measure but he acknowledged that a senator could amend any of the provisions.

On subsection (2) of Section 106(A), Senator Enrile noted that the provision expanded the number of zero-rated transactions by including “the sale of goods, supplies and fuel to persons engaged exclusively in international shipping or

international air transport." He recalled that the Chingkoe trade scam used the tax credits to swindle the government of millions of pesos of tax money. He said that the international shipping company or airline should be the one zero-rated to simplify the operation because the supplier of goods and supplies could be claiming a tax credit from government when there had been no VAT paid. Senator Recto said that in all other countries that have a VAT system, services to an international carrier and the carrier itself are zero-rated. The problem, he pointed out, is on the procedure of getting a tax credit, which could be addressed in the latter sections of the bill.

In reply to another query, Senator Recto explained that under Section 108 (A), airline and shipping industries relative to the transport of passengers, goods and cargoes from one airport or place in the Philippines to another, are subject to VAT. In the past, he said, only cargoes were subject to VAT. Senator Enrile agreed that the provision was an improvement.

On page 6, line 28, asked why "PLACE" was used instead of PORTS, Senator Recto expressed doubt whether there are ports all over the country where these vessels dock. But he expressed willingness to accept an amendment rewording the phrase to AIRPORT, PORT OR PLACE.

On another matter, Senator Recto conceded that the terms "distribution companies" and "electric utilities" might be the same. He agreed to delete one at the proper time.

On the observation that imposing a 10% VAT on electricity would raise the cost of electricity to that extent, Senator Recto explained that precisely, the bill would lower the franchise tax so that the consumer would be spared from 10% electricity rate increase. He added that excise taxes on some petroleum products would also be reduced since gencos use petroleum to generate electricity. He expressed more concern about petroleum which is more inflationary than power even as he agreed that imposing VAT on electricity and petroleum would definitely hit consumers.

As to the purpose of the capitalized sentence on lines 9 to 12 of page 7, Senator Recto explained that VAT is imposed on a service performed in the Philippines or on the point of destination. But he clarified that overseas travel by air or by sea is

subject to VAT. He pointed out that some services which are provided through the Internet may be performed in the Philippines but are consumed abroad. He took note of the argument that once the transmission is done, the service is completed, and he expressed openness to accept an amendment at the proper time.

Asked why services performed for persons doing business outside the Philippines should be zero-rated, Senator Recto explained that the service is like an export similar to an exporter who manufactures goods locally but sells these abroad. He said that call centers fall under this category but overseas call is imposed an overseas communication tax.

However, Senator Enrile disagreed, pointing out that once the call is finished, the service is completed in the Philippines and should be paid for. Similarly, he said, once accountancy service is transmitted through the airwaves, the service is rendered and should be imposed a VAT.

Senator Recto argued that if an export-oriented enterprise is zero-rated, then a service that is earning foreign exchange should also be treated like an export and be VAT-exempt. Moreover, he said, the goods or service is imposed a VAT once it reaches its destination much like imports to the Philippines which are taxed. He reiterated that goods and services consumed domestically are subject to VAT but locally produced products which are exported are not since these are subject to VAT in the country of destination. He stressed that VAT works that way globally.

On another matter, Senator Enrile asked why "vessels" was replaced with PERSONS on line 4 of page 8 of the bill. Senator Recto explained that a service is rendered to a person, for example, a shipbuilding facility that provides repairs to foreign ships docked in the Philippines would be zero-rated. On the observation that a vessel is not a person, he pointed out that a corporation which owns the vessel is a juridical person. He expressed willingness to revisit the provision at the proper time.

Asked why a sixth category was added to the zero-rated list, Senator Recto informed the Body that the bill would put the airline and shipping industries under the VAT system, but the transport of passengers and cargo by air or sea from the Philippines to a foreign country should be zero-rated.

He clarified that there is no prohibition from imposing a VAT on outgoing flights but doing so would make local airlines and shipping lines less competitive.

On exempt transactions, Senator Recto explained that nonfood agricultural products, marine and forest products in their original state, cotton and cotton seeds would be subject to VAT, except copra which is covered in another section.

On whether the importation and sale of coal and other petroleum products would be subject to VAT, Senator Recto replied in the affirmative.

As to lubricating oil, processed gas, and similar products, Senator Recto stated that they are also subject to VAT. But Senator Enrile pointed out that these products are bracketed in the bill, meaning, exempt from coverage. Senator Recto explained that Section 10 speaks of exempt transactions. Further, he clarified that subsection (e) of the present law was deleted and substituted with subsection (C) which provides that the SALE OF NATURAL GAS AND OTHER INDIGENOUS AND RENEWABLE SOURCES OF ENERGY IN WHATEVER FORM OR STATE.

Senator Enrile reasoned that he just wanted to be sure that the words in parentheses under the existing law would not escape the VAT.

On whether the products enumerated under subsection (f) of the code would also be covered by the VAT, Senator Recto replied in the affirmative. He clarified that anything that is not listed is subject to VAT.

Asked if the importation of passenger and cargo vessels of more than five thousand (5,000) tons, whether coastwise or ocean-going, including their engine or spare parts would also be subject to VAT, Senator Recto also replied in the affirmative.

With regard to the importation of aircraft, Senator Recto explained that importation of vessels for domestic use would be subject to tax but if used internationally, it would be partly exempted. He noted that there are airlines that fly the Manila-Cebu-Hong Kong route.

Asked how domestic use is distinguished from international use, Senator Recto replied that the

records of gross sales, flight hours, destinations, etc. of a company could be examined. He further explained that a domestic airline is subject to VAT but an overseas airline is not.

Asked if a 737 airplane imported by PAL would be subject to VAT, Senator Recto replied in the affirmative as he pointed out that PAL could get a tax refund or a tax credit certificate. He affirmed that if PAL uses the plane for domestic flights, the VAT would be applied; however, its income from international operations is not subject to VAT. He said that if PAL used the plane to carry cargo using the Manila-Cebu-Hong Kong route, the transaction would be VAT-free but it would be subject to tax if the cargo was unloaded in Cebu.

Asked if the importation of personal household effects belonging to residents and nonresident citizens resettling in the Philippines is exempt from VAT, Senator Recto replied in the affirmative, but it would not be exempt from the tariff and customs duties if the amount of the goods exceeded P10,000.00.

On whether new personal effects from abroad are also covered by VAT, Senator Recto replied that the Tariff and Customs Code simply speaks of the amount of P10,000.

Asked why personal and household effects are exempt, Senator Recto replied that it is to prevent smuggling but he admitted that it is being abused by *ukay-ukay* owners.

On whether he would agree to the insertion of the word USED before the word "personal," Senator Recto replied that he would not mind if the entire provision was deleted. Senator Enrile argued that whatever little things that could be added to the revenue of the government would be important, considering the financial situation of the Philippines. He said that it would be better to modify rather than to delete the provision because there are Filipinos coming back to the Philippines with their personal and household effects.

As to the difference between the term "personal and household effects" under subsection (D) and the term "personal and household effects" in subsection (E), Senator Recto explained that subsection (D) refers to residents or citizens like the *balikbayans* and subsection (E) refers to foreigners who would like to settle in the Philippines.

He explained that a foreigner who wants to reside in the Philippines could bring his professional equipment, wearing apparel, domestic animal and household effects which would not be subject to VAT but not his vehicle, car, plane, boat, vessel or yacht. Senator Enrile pointed out that the provision has to be improved.

On the medical, dental, hospital and veterinary services mentioned on page 10, line 9, Senator Enrile queried why all are exempt except those rendered by professionals. As an example, Senator Recto cited that a hospital service is not subject to VAT but the doctor's professional service is. Dental, medical and veterinary services, he said, are also not subject to VAT.

Referring to page 11, line 4, Senator Enrile queried why sales to non-members of cooperatives are not subject to VAT. Senator Recto replied that the existing law carries the provision but he has no objection if VAT is imposed on such sales. He noted that there is a portion in the bill where it provides that the original state of agricultural products, whether sold to the cooperative's members or non-members, are exempt from VAT. Senator Enrile stressed that the sale of processed food by agricultural cooperatives to non-members is already engaging in business.

Replying to further queries, Senator Recto said that if the power industry would be covered by VAT, it would have to include the entire chain – the electric utility, electric cooperatives and the like.

Anent line 15 to 17, page 11, Senator Enrile queried why gross receipts from lending activities of credit or multipurpose cooperatives are exempt from VAT. Senator Recto replied that these are exempted because banks are not subject to VAT and the cooperatives are not subject to gross receipts tax either. Senator Enrile argued that there are big lending cooperatives in the country, many of which are affluent. Senator Recto said that as a general rule, lending cooperatives are just small cooperatives and he does not know of one being owned by an affluent person.

Finally, referring to lines 18 to 22, Senator Enrile queried why sales of non-agricultural, non-electric and non-credit cooperatives are to be exempt and what cooperatives are these. Senator Recto replied that it could be any type of cooperative as he clarified that only electric cooperatives are included in the bill.

At this juncture, Senator Enrile made reservation to continue his interpellation at a later day.

SUSPENSION OF CONSIDERATION OF SENATE BILL NO. 1950

Upon motion of Senator Pangilinan, there being no objection, the Body suspended consideration of the measure.

SUSPENSION OF SESSION

Upon motion of Senator Pangilinan, the session was suspended.

It was 7:18 p.m.

RESUMPTION OF SESSION

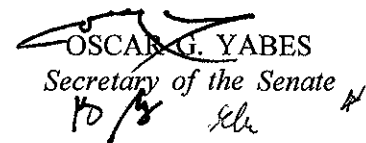
At 7:18 p.m., the session was resumed.

ADJOURNMENT OF SESSION

Upon motion of Senator Pangilinan, there being no objection, the Chair declared the session adjourned until three o'clock in the afternoon of the following day.

It was 7:18 p.m.

I hereby certify to the correctness of the foregoing.


OSCAR G. YABES
Secretary of the Senate

Approved on March 9, 2005