LEGISLATIVE RESEARCH SERVICE
QUICK NOTES
Second Regular Session, 19th Congress

Public Hearing of the Committee on Ways and Means

Chairperson: Sen. Win Gatchalian

28 November 2023, Tuesday, 10:00 a.m., Tolentino Room, Senate

Re: Inquiry on the Apparent Inconsistency between the Create Law and its Implementing Rules and Regulations (IRR)

- **P.S. Res. No. 219—Sen. Risa Hontiveros**
- **P.S. Res. No. 244—Sen. Aquilino "Koko" Pimentel III**
- **P.S. Res. No. 567—Sen. Win Gatchalian**

Background

- Republic Act No. 11534, or the Corporate Recovery and Tax Incentives for Enterprises (CREATE) Law, was approved and passed into law on March 26, 2021. It took effect on April 11, 2021.

- The CREATE Law granted all covered enterprises value-added tax (VAT) exemption from their importations as well as a zero-rating on their domestic purchases.

- Section 294, paragraph (e) of the National Internal Revenue Code (NIRC), as amended by the CREATE Law, provides for **VAT exemption on importation and VAT zero-rating on local purchases**. Conversely, section 295 paragraph (d) of the NIRC, as amended by the CREATE Law, provides that the VAT exemption on importation and VAT zero-rating on local purchases shall only apply to goods and services directly and exclusively used in the registered project or activity by a **registered business enterprise (RBE)**.

- Consequently, on June 21, 2022, the CREATE Law's implementing rules and regulations (IRR) were approved and jointly signed by the Department of Finance and the Department of Trade and Industry. Section 5, Rule 2 thereof states that the VAT exemption on importation and VAT zero-rating on local purchases shall only apply to goods and services directly and exclusively used in the registered project or activity of a **registered export enterprise**.

- Subsequently, the Bureau of Internal Revenue (BIR) issued BIR Revenue Regulations No. 21-2021, which provides that the sale of goods and services to a **registered export enterprise**, to be used directly and exclusively in its registered project or activity pursuant to sections 294 (e) and 295(d) of the CREATE Law, and section 5, Rule 2 of its IRR, shall be subject to VAT zero-rating. The same was further clarified under BIR Memorandum Circular No. 24-2022.

- Pursuant to the IRR, the Clark Development Corporation (CDC) issued Memorandum Circular No. IPDII-22-04-14 notifying Clark Freeport Zone (CFZ) locators that the enjoyment of VAT exemption and zero-rated privileges applies only to export enterprises; that locators not categorized as export enterprises shall revert to being domestic enterprises; and that existing locators may continue to enjoy their gross income earned (GIE) only within the applicable transitory period.

- It is apparent that the interpretation contained in the IRR and Revenue Regulations No. 21-2021 appears to be inconsistent with the language and spirit of NIRC Section 295 (d), as amended, which is to make VAT exemption on importation and zero-rating on domestic purchases available to both export and domestic enterprises.

- For this reason, Senators Risa Hontiveros, Win Gatchalian, and Aquilino “Koko” Pimentel filed their resolutions, which are now under consideration.

Highlights

- Proposed Senate Resolution Nos. 244 and 567 filed by Senators Pimentel and Gatchalian, respectively, direct the Senate Committee on Ways and Means to inquire into the apparent discrepancy between the CREATE Act and its implementing rules and regulations, as well as the related BIR issuances, with focus on domestic market enterprises (DMEs) in economic zones in the resolution filed by Senator Pimentel.

- As stated under P. S. Res. No. 567, because of the erroneous interpretation of the CREATE Law by the BIR, RBEs that are classified as DMEs are not able to avail of VAT exemption and VAT zero-rating that are guaranteed under the CREATE Law. Further, the inconsistencies reduce investors’ confidence.[1] Worse, the CREATE Law’s IRR and the BIR issuances in relation thereto are contrary to the CREATE Law’s policy of promoting global competitiveness, tax incentives uniformity, and fiscal stability for both local and foreign locators.[2]

- As expressed in P. S. Res. No. 244, the CREATE IRR and the BIR issuances, in effect, require suppliers to pass on VAT to locators in the CFZ and other special economic zones, particularly if they are domestic market enterprises and, regardless if they are still currently enjoying the 5% GIE during the transitory period.

- P. S. Res. No. 219, filed by Senator Hontiveros, also calls for the convening of the Congressional Oversight Committee on the Comprehensive Tax Reform Program to remedy the apparent inconsistencies. The resolution takes into account the report of the Fiscal Incentives Review Board (FIRB) that there were

[1] Paraphrased from Proposed Senate Resolution No. 244
[2] I*bid.*

5,520 businesses registered with the various Investments Promotion Agencies (IPAs) before the passage of the CREATE Law, of which 1,391 were domestic enterprises, 3,232 were export-oriented enterprises, and 895 were mixed enterprises. Thus, the deviation of the issuances from the intent of the CREATE Law has directly and adversely affected the cost of doing business for 212 domestic industries while potentially discouraging other domestic firms from registering with IPAs.

Possible Points for Discussion

- **Inconsistencies between the CREATE Law and its IRR, including related BIR issuances:** The implementation of the CREATE Law has revealed certain discrepancies between the law itself and its IRR, including the related issuances by the BIR. These inconsistencies have created confusion and challenges for businesses and taxpayers in understanding and complying with the new tax regime.

- **Data on the number of domestic enterprises adversely affected by the said inconsistencies:** This data would help policymakers understand the practical consequences of these issues on businesses.

- **Current number of businesses registered with IPAs:** To gauge the economic landscape and the potential impact of the CREATE Law, it is essential to have up-to-date data on the number of businesses registered with Investment Promotion Agencies (IPAs). This information can provide insights into the attractiveness of the Philippines as an investment destination, the growth of new enterprises, and the utilization of tax incentives provided under the law.

- **Amendments to the CREATE Law's IRR to reflect the real intent of the law:** Based on the findings regarding inconsistencies and their impact, the concerned authorities must amend the CREATE Law's IRR, rectify the situation, and align the operationalization of the law to its original intent. These amendments should aim to provide clarity, stability, and predictability for businesses while ensuring the government's revenue objectives are met.