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VIA E-MAIL

The Honorable Carlos G. Dominguez
Secretary of Finance
DOF Building, Roxas Boulevard
Manila City, Metro Manila, Philippines
secfin@dof.gov.ph

Re: Statement of Support for Package 4 of the Comprehensive Tax Reform Program ("CTRP"), or the Passive Income and Financial Intermediary Taxation Act ("PIFITA")

Dear Mr. Secretary,

The Association of Global Custodians ("AGC")[1] serves as a non-partisan advocacy organization representing our members' common interests on regulatory and market structure through interaction with legislative and regulatory authorities and financial industry organizations. In 2017, the AGC had submitted a letter [2] to the National Tax Research Center ("NTRC") containing our recommendations for consideration in the development of the tax reform proposals under the Tax Reform for Acceleration and Inclusion Act ("TRAIN 4"). We are encouraged to see the recommendations being reflected in the tax reform proposal that has been tabled to the Senate now.

In this regard, we are writing about Package 4 of the Comprehensive Tax Reform Program ("CTRP"), or the Passive Income and Financial Intermediary Taxation Act ("PIFITA"). We understand that PIFITA through House Bill 304 has passed its Third Reading with the House of Representatives and is currently being transmitted to the

[1] The Association is an informal group of 12 member banks that provide securities safekeeping and asset servicing functions to cross-border institutional investors worldwide, including investment funds. In providing global custody services, AGC members routinely seek appropriate withholding tax relief on behalf of custody clients by processing millions of such claims in the aggregate each year, affecting substantial amounts of cross-border portfolio investment flows in and out of countries worldwide.

[2] AGC letter dated 6 December 2017: http://www.theagc.com/2017-12-06%20AGC%20letter%20to%20Philippines%20re%20TRAIN%204.pdf.

Senate for approval. As it currently stands, the draft PIFITA would introduce a simpler, fairer and more efficient tax system, and we support many of its proposed tax reforms. As PIFITA could not be passed in 2018, we hope that in 2019 it can enjoy a higher level of priority for its review and approval by the Senate so that its proposed tax reforms (with the exclusion of the proposed bond transaction tax) can better amplify its benefits and facilitate new interest in the Philippine capital market.

We would like to laud the efforts to date of the Department of Finance and its various stakeholders in reviewing and refining the country's tax framework, especially in areas that are of utmost relevance to its economy and investors. We thank you for the open communication, which has been valuable in bridging the shared interests of both the Philippines and its non-resident investors that the AGC represents. We look forward to further dialogue and interaction with the common objective of growing the Philippine capital market.

In this letter, we respectfully submit our position on PIFITA, more importantly on why we support its priority review and approval by the Senate, and our reservation on the proposed new bond transaction tax.

1. **The importance of PIFITA and why it should be allocated priority review for approval by the Senate in 2019**

   PIFITA is a comprehensive tax package that aims to simplify and standardize market taxes, which would improve the Philippines' standing in attracting non-resident investments. It brings the Philippines closer to the same competitiveness as India and China[3], which have recently relaxed many of their cross-border restrictions to make it more efficient and easier for overseas investments to flow into their economies.

   We set out the reasons the AGC supports the passage of PIFITA (excluding the bond transaction tax) by the Senate in 2019:

   a) The proposed application of a uniform 15% rate (tax deducted at source), regardless of the type of taxpayer, instrument, currency and maturity, will enhance the Philippine capital market as an investment destination. Presently, the tax structure is particularly challenging for Global Custodians to ensure the correct application of relevant tax rates as their clients are of different investor classifications and tax residency and have varying investment appetites or mandates. A uniform 15% rate will simplify the tax

[3] The Indian Government introduced a series of measures through the Taxation Laws (Amendment) Ordinance, 2019 ("Ordinance") to boost foreign investments. Some of the tax reforms include (i) rolling back the enhanced surcharge on capital gains tax on equities and (ii) withdrawal of buy-back tax in respect of certain listed shares. As for China, on 7 November 2018, China's Ministry of Finance (MOF) and the State Administration of Taxation (SAT) jointly issued Circular [2018] 108 (Circular 108). This gives effect to the 30 August 2018 State Council announcement of a 3-year exemption from corporate income tax withholding tax (WHT) and Value Added Tax (VAT) for China-sourced bond interest derived by overseas institutional investors. The WHT and VAT exemptions apply from 7 November 2018 to 6 November 2021.

structure and can give Philippines a more favorable impression as a place with increased ease of doing business.

b) The Philippines has bilateral tax treaties with 43 countries. The harmonization and reduction of tax rates on dividend and interest income to 15% will remove the administrative burdens on non-resident investors seeking double taxation treaty (DTT) relief on their Philippine income as explained in the following:

- The standard tax treaty rates on dividend income for non-resident portfolio investors in all 43 countries are equal to or higher than the proposed rate of 15%.[4] The reduction of the statutory dividend tax rate for non-residents from 30% to 15% will remove the need for non-resident investors eligible for the standard dividend tax treaty rate to apply for tax treaty relief.

- The standard tax treaty rate on interest income for non-resident investors in 8 out of 43 countries is at 15%. The proposed reduction of the interest income tax rate for non-residents from 20% to 15% will remove the need for non-resident investors in these countries to apply for tax treaty relief. Non-residents in the other 35 countries with DTT may consider no longer pursuing any tax treaty relief through further administration.

c) The proposed phased reduction of the stock transaction tax from 0.6% to 0.1% by 2025 with removal of the transaction tax in 2026 can attract non-resident investors' interest into the Philippine stock market, which has net returns of 13.08%[5] in the past 12 months and 7.35%[6] September YTD 2019 despite the global trade tension. This contrasts favorably with MSCI Emerging Markets net returns of (negative) -2.02% and 5.89% in the respective time periods.

The tax reform can ensure that the Philippine market can continue to grow sustainably in the foreseeable future where global growth is being forecasted to be largely restrained. The stock transaction tax's reduction can make the Philippine equity market more globally competitive; with deeper liquidity and a more diversified investor base that could generate follow-on benefits for the market participants.

Next, we would like to highlight a need to review the proposed transaction tax on debt securities' trading for its exclusion and removal.

[4] The standard tax treaty rate on dividend income excludes non-residents that meet specified ownership criteria and are eligible for the lower value of the tax rate according to the tax treaty with the respective jurisdiction. Link: https://www.dits.deloitte.com/#Jurisdiction/12 shows the countries with tax treaties that contain the ownership criteria.
[5] MSCI Philippines Index (USD), last assessed 20 Oct 2019.
[6] MSCI Philippines Index (USD), last assessed 20 Oct 2019.

2. **Removal of the proposed transaction tax of 0.1% on secondary trading of debt securities ("bond transaction tax")**

   PIFITA presently contains a proposal for a bond transaction tax of 0.1% which will be removed by 2026. We recommend for your favorable review to remove this new bond transaction tax for the following reasons:

   a) This is a new tax for investors of debt securities such as pensions, funds and insurance, which disadvantages them from their investment goals to hold fixed income instruments in favor of their end-beneficiaries like retail investors, pensioners, and insured consumers. The proposed bond tax amplifies the cost on such long-term investors' holdings, which naturally would need to be in large values.

   b) The industry, including offshore agents like global custodians and investors, and the local authorities will need to institute a new range of tax compliance and monitoring processes in order to support the calculation, allocation, collection, submission, filing, auditing, and retention of records of this proposed 0.1% tax.

      Further regulatory work to clarify exact operational requirements will also be needed, for example whether market liquidity enhancing practices like debt repurchases (repos) will also attract this additional 0.1% transaction tax, and which government or official entities would be subjected to this tax, and other considerations. A whole new administration layer will need to be created, which will add new compliance costs that PIFITA is trying to remove.

      Given the proposed time-limited duration of this tax (to be removed by 2026), it is also questionable how much will be invested into automation that will also need time to be developed and tested before being rolled out. This can create new manual work and operational risks.

Due to such added complexity, there may be a negative impact on the level of investment activity on debt securities. We respectfully ask for the reconsideration and retraction of the bond transaction tax.

Again, we thank you for this opportunity to send our views for your consideration as we work together to enhance the Philippine capital market and improve the ease of access it provides to non-resident investors.

Please do not hesitate to contact the undersigned should you have any questions or clarifications.

Thank you.

Sincerely yours on behalf of the Association,

Mary C. Bennett

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