

Republic of the Philippines
HOUSE OF REPRESENTATIVES
Quezon City

Sixteenth Congress
Second Regular Session

HOUSE BILL NO. 5843



Introduced by **REP. CARLOS M. PADILLA**

EXPLANATORY NOTE

The Philippines is one of the most mineral-rich countries in the world. The value of the country's mineral resources is estimated by the Mineral Development Council to be around US\$840 Billion. According to the Mines and Geosciences Bureau (MGB), the country's metallic mineral reserve is about 7.1 billion tons. However, the mining and quarrying sector constitutes the smallest contribution to the total industry, averaging 2.7 percent for the period 1998-2010. In fact, among the economic sectors or industries, mining and quarrying contributed the least to the total economy after forestry, averaging only about 0.9 percent to total GDP during the same period.

Tax administration is also burdensome, specifically in the large-scale metallic mining sector. Different contracts are governed by varying fiscal regimes depending on where it is operating and whether it is operating under a Mineral Production Sharing Agreement (MPSA) or Financial and Technical Assistance Agreement (FTAA). To date, almost all mining contracts are under MPSA, while those in mineral reservations are composed mainly of nickel mines. All FTAA agreements are for mines outside mineral reservations.

More specifically, the current fiscal regime can be described as follows:

1. Only mines operating in a mineral reservation pay the royalty – 5 percent of the market value of gross output, and the only companies currently mining in a mineral reservation are all operating under an MPSA.
2. All mines pay the 2 percent excise tax, which is also levied on the market value of gross output.
3. In addition to the excise and possible the royalty, MPSAs pay national taxes including corporate income tax, withholding taxes, customs duties, and VAT.

4. Miners also pay real property tax, local business taxes and fees, and additional royalty for indigenous peoples for projects within ancestral domain areas.
5. The FTAA, on the other hand, is structured in two components: the basic government share and the additional government share. The basic government share includes the same national taxes, local taxes, and fees paid by MPSAs. The additional government share, which is paid after the recovery period, is equal to 50 percent of net mining revenue in excess of the basic government share.

This bill is proposed to implement a single fiscal regime applicable to all large scale metallic mining to address the complex and differentiated fiscal regime. It also proposes for a reasonable increase in government share from the extraction of metallic mineral resources.

The proposed bill imposes a mineral royalty of 5 percent in addition to the excise tax and other national and local taxes collected by the national and local governments.

In addition to the corporate income tax and royalty, a 10 percent surcharge on cash flow is proposed to serve as the additional government share when prices of mineral products are on the upswing. Under the present fiscal regime, the government does not get an additional share during higher prices due to the absence of a fiscal instrument that allows government to share during high prices. Moving forward, the 10 percent surcharge should be an important feature of the mining fiscal regime.

Also, as the mining industry is heavily dependent on the presence of natural resources to be extracted, the bill proposes to eliminate all tax incentives to be given to mining companies. Incentives are not needed to be given to ensure investment in the mining sector.

Measures for thin capitalization is also introduced to control the businesses not to rely on excessive debt funding which results in higher interest expense deductions. Thin capitalization occurs when investors rely on excessive debt funding and little equity funding to reduce corporate tax liability. It would be better and simpler for the limit on excessive debt to apply to all loans so as to avoid intricate tracking of loans whether it is from related party or subsidiary.

Another steering measure to attain optimal goal of the government in maximizing its share is the overture of "ring fencing" per project. Ring fencing prevents the consolidation of income and expenses across mining projects by the same taxpayer.

Ring fencing limits the consolidation of income and tax deductions from exploration and development expenditures for different activities and projects undertaken by the same investor. This means that losses from other mining projects are prevented from being deducted from projects that are more profitable. Ring fencing is particularly important for any profit-based additional tax such as the 10 percent surcharge of cash flow. A taxpayer that operates more than one taxable entity would be assessed for additional tax on each separately.

To further maximize the benefit from mining, an export tax of 5% on gross value of production of raw ore is proposed. This will encourage the development of higher value-added downstream industries which will bring additional benefits of mining to the country.

This bill also proposes to increase the share of local governments from the extraction of mineral resources. Except for Zambales, Benguet and Palawan, our mining provinces are also among the provinces with highest incidence of poverty among families. The additional share from the extraction of resources from these provinces will provide them with additional funds for social and economic development.

Recognizing intergenerational equity and ensuring that mining contribute to sustainable and long-term development, the proceeds from the extraction of minerals are to be earmarked to augment the fund the national and local governments are allocating for education, health, environmental management and other similar programs. The proposed bill also requires the national and local governments to create a natural resource trust fund to efficiently manage the proceeds from mining.

To ensure transparency and accountability of the extractive industry, the Philippine Extractive Industry Transparency Initiative is hereby created under the Office of the President. Among the mandates of PH-EITI is to monitor the payments and fees paid by extractive companies, monitor the utilization of proceeds from extractive industries and facilitate access to information regarding extractive industries.

In light of the foregoing, the passage of this bill is earnestly sought.


CARLOS M. PADILLA

Republic of the Philippines
HOUSE OF REPRESENTATIVES
Quezon City

SIXTEENTH CONGRESS
First Regular Session

House Bill No. **5843**

Introduced by Rep. CARLOS M. PADILLA

**AN ACT PROVIDING FOR THE RESTRUCTURING OF THE FISCAL REGIME
FOR MINERALS AND MINERAL PRODUCTS AND QUARRY RESOURCES**

Be it enacted by the Senate and the House of Representatives of the Philippines in session assembled:

GENERAL PROVISIONS

SECTION 1. Title. This act shall be known the "Fiscal Regime for Mineral and Mineral Products and Quarry Resources."

SECTION 2. Declaration of Principles.

- A. All mineral resources within the territory and exclusive economic zone of the Republic of the Philippines are owned by the State. It shall be the responsibility of the State to promote their rational exploration, development, utilization and conservation through the combined efforts of government and the private sector in order to enhance national growth in a way that effectively safeguards the environment and protect the rights of affected communities.
- B. The Philippines is one of the most mineral-rich countries in the world. As such, the state must establish a fiscal regime that allows a fair and equitable sharing of revenues and any economic benefits derived from mineral resources, not just on the national level, but also on the local level.

SECTION 3. Definition of Terms.

- A. **"Arm's Length Debt Amount,"** in relation to a mining contractor, means the amount of debt that a bank that is not an associate of the contractor would be prepared to lend to the contractor;

- B. **"Cash Flow Surcharge"** refers to a surcharge to be imposed on the cash flows of each mining area for each taxable fiscal year;
- C. **"Contract Area"** means the land or body of water delineated under a Mineral Agreement or a Financial or Technical Assistance Agreement (FTAA) of the Contractor and properly defined by longitude and latitude;
- D. **"Contractor"** means a Qualified Person, as defined in Department Order 2012-21 of the Department of Environment and Natural Resources, acting alone or in consortium who is a party to a Mineral Agreement or FTAA;
- E. **"Debt,"** in relation to a mining contractor, means the greatest amount, at any time during a taxable fiscal year, of the debt obligations of a contractor on which interest is made payable as determined according to international financial reporting standards;
- F. **"Extractive Industries"** refer to the mining, oil, gas and coal sectors and all other sectors that require the extraction of non-renewable natural resources for commercial use;
- G. **"Financial or Technical Assistance Agreement (FTAA)"** means a contract involving financial or technical assistance for large-scale exploration, development and utilization of mineral resources;
- H. **"Gross Output"** means the actual market value of minerals or mineral products from each mine or mineral land operated as a separate entity, without any deduction for mining, processing, refining, transporting, handling, marketing or any other expenses;
- I. **"Mineral Agreement"** means a contract between the Government and a Contractor, involving Mineral Production Sharing Agreement, Co-Production Agreement or Joint Venture Agreement;
- J. **"Mining Area"** refers to a portion of the contract area identified by the Contractor as defined and delineated in a Survey Plan duly approved by the Director/Regional Director concerned for purposes of development and/or utilization, and sites for support facilities;
- K. **"Minerals"** refer to all naturally occurring inorganic substances in solid, liquid, gas or any intermediate state excluding energy materials such as coal, petroleum, natural gas, radioactive materials and geothermal energy;

- L. **"Mineral Products"** mean materials derived from ores, minerals and/or rocks and prepared into a marketable state by mineral processing;
- M. **"Mining Operations"** mean mining activities involving exploration, feasibility study, development and utilization;
- N. **"Quarry Resources"** refers to any common rock or other mineral substances as the Director of Mines and Geosciences Bureau may declare to be quarry resources such as, but not limited to, andesite, basalt, conglomerate, coral sand, diatomaceous earth, diorite, decorative stones, gabbro, granite, limestone, marble, marl, red burning clays for potteries and bricks, rhyolite, rock phosphate, sandstone, serpentine, shale, tuff, volcanic cinders, and volcanic glass: Provided, That such quarry resources do not contain metals or metallic constituents and/or other valuable minerals in economically workable quantities: Provided, further, That non-metallic minerals such as kaolin, feldspar, bullquartz, quartz or silica, sand and pebbles, bentonite, talc, asbestos, barite, gypsum, bauxite, magnesite, dolomite, mica, precious and semi-precious stones, and other non-metallic minerals that may later be discovered and which the Director declares the same to be of economically workable quantities, shall not be classified under the category of quarry resources;
- O. **"Separate Taxable Person or Personality"** refers to an independent taxable entity as determined by business operations in a specific mining area;
- P. **"State"** means the Republic of the Philippines;
- Q. **"Taxable Fiscal Year"** means an accounting period of twelve (12) months depending on the accounting method of the Contractor;
- R. **"Utilization"** means the extraction, mineral processing and/or disposition of minerals.

SECTION 4. Interpretation. Nothing in this Act shall be construed as a diminution of the rights and privileges of local government units presently enjoyed under existing laws such as Republic Act No. 7160 of 1991. Nothing in this Act shall be construed as a diminution of the rights enjoyed by indigenous peoples under the Indigenous Peoples' Rights Act of 1997.

CHAPTER II

SCOPE AND APPLICATION

SECTION 5. Scope and Application. This Act shall and apply to new Mineral Agreements and FTAA's covering large-scale mineral mining operations that are entered into upon the effectivity of the Act. This shall also cover existing Mineral Agreements and FTAA's where such agreements provide that any terms and conditions resulting from repeal or amendment of any existing laws or regulation or from the enactment of a law, regulation or administrative order shall be considered a part of said agreements.

The renewal and renegotiation of existing Mineral Agreements and FTAA's shall also be governed by this Act.

CHAPTER III

TAXATION OF MINERALS, MINERAL PRODUCTS, AND QUARRY RESOURCES

SECTION 6. Separate Taxable Personality. Each mining operation in a mining area will be considered a separate taxable entity. If a mining contractor is party or holds more than one mineral agreement, he shall be treated as a separate person in respect of the business operations related to each mining area.

SECTION 7. Mining Royalty. There shall be levied assessed and collected on minerals, mineral products and quarry resources a mineral royalty of five percent (5%) based on the market value of the gross output at the time of sale; or the value used by the Bureau of Customs in determining tariff and custom duties.

SECTION 8. Cash Flow Surcharge. A surcharge of ten percent (10%) shall be imposed on the cash flows of each mining area for every taxable fiscal year. For purposes of the cash flow surcharge (CFS), each mining area shall be considered a separate taxable entity. The tax base of the CFS is determined by adding back the depreciation and interest expense and other financing charges to the regular taxable income used for the purposes of the corporate income tax, before the loss carryover, and before deducting any capital expenditure and the regular corporate income tax. Any surcharge loss is carried forward to subsequent years so as to avoid charging the CFS until the mining area has a positive cash flow.

SECTION 9. Limitations on Deductions for Purposes of Computing the CFS. When computing for the cash flow surcharge, mining companies must adhere to the following guidelines:

- A. A deduction for expenses or losses incurred, wholly or partly, by a contractor in undertaking mining operations in a mining area during a taxable fiscal year is allowed only against the income derived by the contractor from such operations in the mining area during the same taxable fiscal year.
- B. If the total deductions in respect of the mining operations undertaken by the contractor in a mining area during a taxable fiscal year exceed the total taxable income derived from the same year, the excess may be carried forward and allowed as a deduction against the taxable income of the contractor from mining operations in the mining area for the next taxable fiscal year.
- C. An amount that is not deducted under subsection B may be carried forward to the next taxable fiscal year and allowed as a deduction in accordance with subsection B for that year and so on until the amount has been fully deducted, or until the mining operations in the mining area has ceased.
- D. If a contractor has an excess carried forward under subsection B for more than one fiscal year, the excess of the earliest period is allowed as a deduction first.
- E. If a contractor has ceased mining operations in a mining area and the contractor has a loss under subsection B in relation to the mining area, the contractor may elect, by notice in writing to the BIR Commissioner, to treat the loss as a loss under subsection B in relation to another mining area operated by the contractor, provided that the latter mining area falls wholly within the same contract area of the first-mentioned mining area.
- F. If a contractor has ceased mining operations in a mining area or if the contractor has a loss under subsection B in relation to the mining area and subsection E does not apply to the contractor, the contractor may elect, by notice in writing to the BIR Commissioner, to treat the loss as a loss under subsection B in relation to mining operations undertaken by the contractor in another contract area.

SECTION 10. Limitations on Interest Expense Deductions. The following are limitations on mining contractors for any interest expense deductions:

- A. If a contractor has a debt-to-equity ratio in excess of 1.5 to 1 at any time during a taxable fiscal year, a deduction on the interest paid by the contractor on the portion of the debt which exceeds the 1.5 to 1 ratio for that same fiscal year shall not be allowed.

- B. If the debt-to-equity ratio of a contractor exceeds the 1.5 to 1 ratio for a taxable fiscal year, subsection A will not apply, provided, that during the said fiscal year, the amount of the debt of the contractor should not exceed the arm's length debt amount.

SECTION 11. Export tax on raw ore. An export tax of 5% on the gross value of raw ore exported is hereby imposed to encourage the processing of raw ore in the country;

SECTION 12. Incentives. All tax incentives granted to mineral mining and quarry contractors shall be repealed upon effectivity of this Act.

CHAPTER IV ALLOCATION OF PROCEEDS FROM THE DEVELOPMENT OF THE NATIONAL WEALTH

SECTION 13. Share of Local Government Units (LGUs). The local government unit hosting the mining area shall have an equitable share in the proceeds derived from the utilization and development of the national wealth, including sharing the same with its inhabitants by way of direct benefits.

- A. A local government unit shall, in addition to the internal revenue allotment, have a share of fifty percent (50%) of the gross collection derived by the national government from the preceding fiscal year from excise taxes, royalties and such other taxes, fees or charges, including related surcharges, interests or fines, and from its share in any co-production, joint venture or production sharing agreement in the utilization and development of the national wealth within their territorial jurisdiction. The 50% share shall be distributed among LGUs according to the Local Government Code of 1991 and its implementing rules and regulations. Provided that in the event that an operation is hosted by several local government units, the share shall be divided equitably among the host local government units based on the amount of ore extracted from the local government unit.
- B. The Bureau of Internal Revenue (BIR) is given the authority to inspect mining sites and monitor the amount of minerals extracted by companies. The BIR, the Mines and Geosciences Bureau (MGB) and the Philippine Port Authority (PPA) shall reconcile their figures on the amount and value of minerals that were actually extracted and exported by companies. The reconciled figure will be the basis for taxation and allocation of share among units of governments.

- C. With respect to payment of business tax, 80% of the payment shall go to the local government unit hosting the mining operation and the 20% the payment shall go to the local government unit where the main office of the business is located. If the mining operation is hosted by several local government units, the 80% shall be shared equally by the said LGUs.

SECTION 14. Natural Resource Trust Fund. To ensure intergenerational equity and transparency and accountability in the use of proceeds from the extraction of mineral resources, the national and local governments shall create a natural resource trust fund where all the proceeds from the mining activities including local taxes shall accrue.

- A. The proceeds may be used by the national and local governments to support educational
- B. and health services and natural resource protection and management.
- C. The local governments may invest the money in the trust and shall not be required to return the balance of the trust to the national government at the end of every fiscal year.

CHAPTER V MONITORING

SECTION 15. Creation of the Philippine Extractive Industries Transparency Initiative or PH-EITI. There is hereby created the Philippine Extractive Industries Transparency Initiative (hereinafter referred to as PH-EITI), a multi-stakeholder group tasked to implement the EITI standards of transparency and accountability in the extractive industries.

SECTION 16. Composition. In accordance with the EITI International Standards, the PH-EITI shall be implemented by a multi-stakeholder group (MSG) and shall consist of representatives from the following sectors:

- A. Government Representatives. The government representatives shall be composed of senior officials from concerned agencies including representatives from local governments. Representatives from Congress shall also be included to ensure that the findings of EITI will inform policy making;

- B. Industry Representatives. The industry representatives shall be composed of officials from the extractive industries included in the EITI; and
- C. Civil Society Organizations (CSOs) Representatives. The civil society shall independently select their representatives in the EITI.

The composition and number of representatives shall be subject to regular review by the MSG. Other agencies may form part of the MSG subject to the evolving needs and scope of the EITI implementation, provided that all sectors should be adequately represented in the MSG at all times. Provided that the existing PH-EITI created under Executive Order no. 147, s. 2013 shall be constituted under the provisions of this Act.

SECTION 17. Powers and Functions. The PH-EITI MSG shall perform the following functions:

- A. Ensure sustained political commitment for the initiative and mobilize resources to sustain its activities and goals;
- B. Set the strategic direction required for effectively implementing the initiative in the Philippines;
- C. Assess and seek the removal of barriers to its implementation;
- D. Set the scope of the EITI process; and
- E. Ensure that the initiative is effectively integrated in other related government reform agenda.

SECTION 18. PH-EITI Office. There is hereby created a PH-EITI Office under the Office of the President. The PH-EITI Office shall be headed by an Adviser as appointed by the President of the Philippines. The MSG shall then select a National Coordinator who will lead the PH-EITI Secretariat team. The MSG shall approve the staffing pattern of the EITI Office and determine the duties, qualifications, responsibilities and functions, as well as the compensation scheme for the positions to be created, upon the recommendation of the National Coordinator. It shall also prepare and approve its work and financial plan. For this purpose, the creation of the corresponding *plantilla* positions is hereby authorized.

SECTION 19. Funding. The Congress shall allocate funding for PH-EITI implementation, including participation of relevant stakeholders from non-government organizations, in the General Appropriations Act.

PH-EITI shall have the authority to receive, disburse, and manage financial aid or grants from foreign and domestic entities to be utilized for the implementation of its objectives subject to the usual accounting and auditing rules and regulations

SECTION 20. Monitoring of Payment and Utilization of Taxes, Fees, Surcharges, Interest and Similar Charges. The payment and utilization of taxes, fees, surcharges, interests, and similar charges made by extractive companies and/or contractors shall be closely monitored by the Philippine Extractive Industries Transparency Initiative or PH-EITI. All fiscal payments shall be disclosed to the PH-EIT

I Multi- Stakeholder Group for the production of the annual EITI report. National and local governments are required to report how the proceeds from mining were utilized.

SECTION 21. Exemption from Confidentiality Clauses. Confidentiality provisions stated under Section 270 of the National Internal Revenue Code and Article 81 of the Omnibus Investments Code shall not be applicable to extractive companies insofar as their participation in the EITI process is concerned.

SECTION 22. Penalties. Failure to participate in PH-EITI shall be a ground for suspension of the contractor's permit to operate and blacklisting for future projects. A contractor who, without justifiable cause, unreasonably delays or causes the delay of submission of the reporting template within the deadline set by PH-EITI, shall be imposed a fine of One Hundred Thousand Pesos (Php 100,000.00). Sanctions provided for under this Act shall be imposed by the Mines and Geosciences Bureau and or Department of Energy, as the case may be, pursuant to these agencies' internal rules and regulations.

CHAPTER VI TRANSITORY AND MISCELLANEOUS PROVISIONS

SECTION 23. Implementing Rules and Regulations. The Secretaries of Budget and Management, Finance, Trade and Industry, Environment and Natural Resources, and Interior and Local Government, shall, promulgate the necessary rules and regulations for the effective implementation of this Act.

SECTION 24. Separability Clause. If any provision of this Act is declared unconstitutional or invalid, other parts or provisions hereof not affected thereby shall continue to be in full force and effect.

SECTION 25. Repealing Clause. All laws, decrees executive orders, rules and regulations or parts thereof which are contrary to or inconsistent with Act are hereby repealed, amended or modified accordingly. *Provided* that nothing in this Act shall be

construed as a diminution of local autonomy or in derogation of ancestral domain rights under the Indigenous Peoples' Rights Act of 1997.

SECTION 26. Effectivity. This Act shall take effect fifteen (15) days after its publication in this Official Gazette or in any two newspapers of general circulation.

Approved.