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Clarifying the VAT provisions of the renewable energy law

In the historic Paris climate agreement to which the Philippines is a signatory, countries have agreed to hold the increase in global average temperature to below 2°C and to pursue efforts to limit the temperature increase to 1.5°C. In order to meet this commitment, the Philippines has to transition to a clean energy economy through investments in renewable energy (RE). Although we have seen in recent years a boost in RE development, further investments in the sector are threatened by the lack of clarity over the tax provisions of Republic Act 9513, or the Renewable Energy Act of 2008 (RE law), in particular, the value-added-tax (VAT) zero-rating of purchases.

A VAT zero-rated transaction pertains to a sale by a VAT-registered person, which is subject to a zero- percent rate, meaning the tax burden is not passed on to the purchaser. A zero-rated sale does not result to any output tax, which is the VAT on the sale of taxable goods or services. However, in a zero-rated sale, the input tax or the VAT paid on importations of goods or local purchases of goods or services can be claimed as a tax credit or refund.

Under the Tax Code and as reiterated in the RE law, the sale of power generated through renewable sources of energy is considered zero-rated. Thus, no output tax can be passed on

by RE developers to the purchaser, i.e. transmission companies. As the sale is zero-rated, the RE developer should be entitled to claim as a tax credit or refund the input tax on its importations of goods or local purchases of goods or services. However, under the same provision, the RE law states that all RE developers shall be entitled to “zero-rated VAT on its purchases of local supply of goods, properties and services needed for the development, construction and installation of its plant facilities”. Moreover, the law provides that the provision applies to “the whole process of exploring and developing RE sources up to its conversion into power, including, but not limited to, the services performed by subcontractors and/or contractors”. Otherwise stated, the sale that the local supplier of goods, properties and services needed for the development, construction and installation of plant facilities and for the exploration and development of the RE source is zero-rated and, thus, no VAT should be passed on by the local RE supplier to the RE developer.

In recent decisions, however, the Court of Tax Appeals has held that, since no VAT should have been shifted to the RE developer for above-mentioned purchases and, consequently, no input VAT should have been paid, a RE developer is not entitled to refund or tax credit in the event the VAT is passed on to it. Further, in one case, the said doctrine was applied to include the VAT paid on importations.

On the issue of whether a RE developer can claim VAT shifted to it by local RE suppliers, the above doctrine should be revisited. While indeed purchases from local RE suppliers are zero-rated, the RE developer should not be barred from claiming any VAT passed on to it. In one case, the Supreme Court has said that if excise taxes, an indirect tax, is shifted by the seller to the buyer, the buyer must be allowed to claim the tax refund or tax credit even if it is not the statutory taxpayer and only bears the economic burden of the tax. VAT is, likewise, an indirect tax, and there is no reason why the same should not apply.

On the issue of VAT paid on importations, the RE law is clear-cut in stating that what are subject to a VAT zero-rate are the purchases from “local” RE suppliers. A perusal of the RE law would show the intent of the legislature to promote the development of local RE suppliers. This explains why there is no mention of importations being subject to a zero-rate or even to an exemption from VAT, as this would benefit foreign RE suppliers.

To include the importations within the coverage of zero-rating not only goes against the clear provisions of the RE law but likewise creates an absurdity, as it conflicts with the “destination principle”, which serves as the basis of our VAT system. Under this principle, goods and services are taxed only in the country, where they are consumed and, thus, exports are zero-rated, while imports are taxed.

In addition, it must be emphasized that zero-rating applies only to “local” purchases of goods, properties and services needed for the development, construction and installation of plant facilities, and for the exploration and development of the RE source. It follows then that local purchases not related to the same remain to be subject to 12-percent VAT and, thus, can be claimed for refund or tax credit.

In sum, RE developers should be able to claim as tax refund or tax credit the VAT paid on their purchases from local RE suppliers where VAT has been passed on, the VAT paid on their purchases unrelated to RE and most especially the VAT paid on their importations.

Developing RE resources is costly and, thus, the need for incentives that make investing in clean energy attractive. Such incentives are already in the RE Law but the uncertainty created by recent CTA decisions as to what previously seemed to be clear VAT provisions are making both current and prospective RE developers think twice.

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