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**TRABAHO bill**
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To complement the Tax Reform for Acceleration and Inclusion law (TRAIN), the House of Representatives just passed on second reading House Bill No. 8083. It contains the Duterte administration's 2nd tax reform package which will be known as "*Tax Reform for Attracting Better and High-quality Opportunities*" or "TRABAHO."

Unlike TRAIN which focused on personal taxes, the TRABAHO bill deals with corporate taxation. Specifically, it aims to reduce the corporate income tax rate from 30% to 20%. Simultaneously, the TRABAHO bill intends to broaden the tax base (revenues subjected to tax) by setting stricter rules on availment of preferential tax rates and some deductions under the Tax Code. The Bureau of Internal Revenue (BIR) Commissioner's power over related-party transactions will also be enhanced.

Another significant part of TRABAHO bill is the rationalization of tax incentives by making them performance-based, targeted, time-bound and transparent. Particularly, TRABAHO bill provides that only those activities included in the Strategic Investment Priorities Plan (SIPP) may be granted tax incentives. There will also be one a single menu of income, customs duty and value-added tax (VAT) incentives.

## REDUCTION OF CORPORATE TAX RATE

Currently, the corporate income tax rate is 30%. Under TRABAHO bill, the rate will gradually reduce by 2% every two years starting 2021 until 2029 when the rate will only be 20%.

## BROADENING OF TAX BASE

To compensate the projected revenue loss resulting from lowering of corporate income tax rate, TRABAHO bill seeks to broaden the tax base by amending several provisions of the Tax Code.

### 15% Gross Income Tax Option

At present, Tax Code gives a corporation the option to be taxed at 15% based on gross income. Under TRABAHO bill, this will no longer be available starting 2019.

### 10% Tax on Proprietary Educational Institutions and Hospitals

Proprietary educational institutions and hospitals which are non-profit enjoy a preferential income tax rate of 10%. Under TRABAHO bill, the availment of this preferential rate will be subject to compliance with established performance criteria to be determined by the Commission on Higher Education (CHED), Department of Education (DepEd), and Department of Health (DOH). Otherwise, they may be subjected to higher income tax rate at 15% or 20%.

### 10% Tax on Regional Operating Headquarters of Multinational Companies

Two years after the effectivity of the proposed TRABAHO law, the 10% preferential tax on regional operating headquarters (ROHQ) will no longer be available.

**Accelerated Depreciation for Private Educational Institutions**

Normally, capital expenses are not deductible outright in one taxable year. Instead, they are deductible gradually by way of yearly allowance for depreciation. However, when a private educational institution incurs a capital expense for expansion of school facilities, it has the option to deduct the capital expense outright.

Under TRABAHO bill, educational institutions can avail of the outright expense option only if they have met the criteria set by CHED, DepEd and DOH.

**Optional Standard Deduction**

In income taxation, it is a basic rule that deduction or expense must be supported with adequate records. However, when a taxpayer chooses optional standard deduction (OSD) over itemized deduction, the requirement of substantiation becomes irrelevant.

At present, the OSD rate for individual and corporate taxpayers is the same at 40% but the bases are different. For individuals, the OSD is applied on the gross sales or receipts (**before** deduction of cost of sales/services). On the other hand, for corporations, OSD is applied on gross income (**after** deduction of cost of sales/services).

Under TRABAHO bill, the 40% OSD rate and base will be uniform for individual and corporate taxpayers at 40% of gross income. However, for corporations, availment of OSD will be limited to those classified as micro, small and medium-sized enterprises as determined by the Department of Trade and Industry.

**Related Party Transactions**

When a transaction is between or among related parties (affiliated/sister companies), businesses have a tendency to arrange the transactions in such a way that their over-all after-tax income is maximized. Thus, related-party transactions are sometimes done not at arm’s length.

To address this gap, the current Tax Code empowers the BIR Commissioner to distribute, apportion or allocate gross income or deductions between or among related parties if the Commissioner finds that such distribution, apportionment or allocation is necessary to **prevent evasion of taxes** or clearly to reflect the income of the taxpayer concerned.

Under TRABAHO bill, the Commissioner will have an enhanced power to distribute, apportion or allocate gross income or deductions as he can exercise it not only to prevent evasion of taxes but also to **prevent avoidance of taxes**.

Moreover, if the transaction or arrangement between or among related parties has the purpose or effect of tax avoidance, the Commissioner may disregard and consider such transaction as void for income tax purposes.

## RATIONALIZATION OF TAX INCENTIVES

Another major purpose of TRABAHO bill is to rationalize tax incentives. Under the bill, only those projects listed in the Strategic Investments Priority Plan (SIPP) may be registered and given incentives.

### Strategic Investments Priority Plan

Every three years, the BOI will formulate a SIPP for approval of the President. In crafting the SIPP, the BOI shall consider, among others, the following:

1. Substantial amount of investments:
2. Considerable generation of employment:
3. Adoption of inclusive business activities and value-added production by MSMEs;
4. Use of modern or new technology;
5. Adoption of adequate environmental protection systems;
6. Address missing gaps in the supply/value chain or move up the value chain or product ladder; or
7. Promotion of market competitiveness.

### Single Incentive Menu

At present, the incentives given to investors depend on the law creating the Investment Promotion Agency (like PEZA, BOI, etc.) granting the incentives. In TRABAHO bill, there will be one single incentive menu for income, customs duty and VAT incentives.

***-Income Tax Incentives***

1. Income Tax Holiday (ITH).- The ITH shall be granted for a period not exceeding three (3) years: provided, that after the expiration of the ITH, the other income tax incentives may be applied for a period not exceeding 5 years, which includes the period of ITH availment.

2. Other income tax incentives include:

    a. Reduced corporate income tax of 18%;
    b. Depreciation allowance for qualified capital expenditure;
    c. Up to 50% additional deduction on the increment of direct labor expense;
    d. Up to 100% additional deduction on research and development expenses;
    e. Up to 100% additional deduction on training expenses;
    f. Up to 100% deduction on infrastructure development;
    g. Deduction for reinvestment allowance to manufacturing industry;
    h. Enhanced net operating loss carry over (NOLCO) wherein the NOLCO during the first 3 years may be carried over within the next 5 years following the year of such loss.

***-Customs Duty Incentives***

Exemption from customs duty on importation of capital equipment and raw materials directly and exclusively used in the registered activity for a period not exceeding 5 years.

***-VAT incentives***

Registered export enterprise whose export sales meet the 90% threshold and are located within an ecozone, freeport, or those utilizing customs bonded manufacturing warehouse may be given VAT zero-rating on export sales, or on importation or domestic purchases of capital equipment and raw materials used in the manufacture and processing of products.

## INCENTIVES GRANTED PRIOR TO EFFECTIVITY OF TRABAHO

With the rationalization of tax incentives, it is important to ask: what will happen to incentives granted prior to effectivity of the proposed TRABAHO law?

The existing registered activities granted the ITH shall be allowed to continue availing the same for its remaining ITH period or for a period of five (5) years only, whichever comes first. If other tax incentives are granted to existing registered activities, such as the five percent (5%) tax on gross income earned (5% GIE), they shall be allowed to continue enjoying the 5% GIE, as follows:

1. Two (2) years for activities enjoying the tax incentive for more than ten (10) years;
2. Three (3) years for activities enjoying the tax incentive between five (5) and ten (10) years; and
3. Five (5) years for activities enjoying the tax incentive below five (5) years.

Provided, that the 5% GIE shall commence after the ITH period has lapsed [but] only for the remaining years within the five-year period.

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*This article is for general information only and based on author's own understanding of the TRABAHO bill. If you have any question or comment regarding this article, you may email the author at egialogo@gdlaw.ph*

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