

Tax Implications of Republic Act Nos. 11600¹ and 11601^{2*}

I. FEATURES

Republic Act (RA) No. 11600 granted the Maynilad Water Services, Inc. (MWSI) a 25-year franchise to establish, operate, and maintain for commercial purposes and in the public interest, a waterworks system to ensure an uninterrupted and adequate supply and distribution of potable water for domestic, commercial, and other purposes, and for the establishment and maintenance of sewerage system and sanitation services in the West Zone Area of Metro Manila and the Province of Cavite, under a concession from the Metropolitan Waterworks and Sewerage System (MWSS), or an appropriate certificate of public convenience and necessity (CPCN), license, or permit from the Regulatory Office established under the Concession Agreement or its legal successor, as may be created or reorganized by executive order or by law.

Similarly, RA 11601 granted the Manila Water Company, Inc. (MWCI) a 25-year franchise to establish, operate, and maintain the waterworks and sewerage system in the East Zone Area of Metro Manila and the Province of Rizal.

The Concession Agreements of the MWSI and MWCI with the MWSS shall serve as the grantees' CPCN, license, or permit to operate its waterworks and sewerage system. Section 5 of both laws authorize the MWSS to approve the amendment of the Concession Agreements to extend its term up to the period of the franchise when public interest for affordable water security so requires, and upon the grantee's application.

With regard to tariffs, rates, and other charges, Section 8 of both laws states that they must remain fair and reasonable to ensure economic viability and a fair return on investments. It shall be based on and consistent with a rate-setting methodology that the Regulatory Office shall define and publish after consultation with stakeholders.

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¹ Entitled, "An Act Granting Maynilad Water Services, Inc. a Franchise to Establish, Operate, and Maintain a Waterworks System and Sewerage and Sanitation Services in the West Zone Service Area of Metro Manila and Province of Cavite", (December 10, 2021).

² Entitled, "An Act Granting Manila Water Company, Inc. a Franchise to Establish, Operate, and Maintain the Waterworks and Sewerage System in the East Zone Service Area of Metro Manila and Province of Rizal", (December 10, 2021).

Under Section 23 of the franchise laws, MWSI and MWCI shall be liable to pay the same taxes on their real estate, buildings, and personal property as other persons or corporations which are now or hereafter be required by law to pay. The grantees, their successors, or assignees shall continue to be liable for income taxes payable under Title II of the National Internal Revenue Code (NIRC) of 1997, as amended. In no case shall the income taxes due from the grantee, its successors, and assignees be passed on to their consumers.

The grantees shall file the return with and pay the tax due thereon to the Commissioner of Internal Revenue or his duly authorized representative in accordance with the NIRC of 1997, as amended, and the return shall be subject to audit by the Bureau of Internal Revenue (BIR).

II. IMPLICATIONS

In general, a franchise is a right, privilege, or power of a public concern which ought not to be exercised by a private individual at his will and pleasure but should be preserved for public control or administration either by the government directly or by public agents under such conditions and regulations as the government may impose in the public interest and for the public security. The essential element of a franchise is that it would be a privilege, right, or power which the individual cannot exercise as of right and which depends for its lawful existence upon a grant from the government.³ While a franchise tax, on the other hand, is a charge imposed in consideration of granting a franchise, operative because the person taxed assents expressly or impliedly.⁴

The MWCI and MWSI are private business entities that provide water and water services in the country. The MWCI exclusively provides services to the East Zone of Metro Manila and Rizal Province, while the MWSI offers services to the West Zone of Metro Manila (See Table 1). They are responsible for operating and improving waterworks systems in conformity with a Revised Concession Agreement they entered into with the MWSS, which is a government corporation that owns and/or has jurisdiction, supervision, and control over all waterworks and sewerage systems in Metro Manila, Cavite, and Bulacan pursuant to Republic Act (RA) No. 6234.⁵

³ Jose Agaton R. Sibal, *Philippine Legal Encyclopedia*, Central Lawbook Publishing Co., Inc., 1986.

⁴ In *Panay Electric Company vs. Commissioner of Internal Revenue*, L-10574, May 28, 1958.

⁵ Entitled, "An Act Creating the Metropolitan Waterworks and Sewerage System and Dissolving the National Waterworks and Sewerage Authority; and for Other Purposes", (June 19, 1971).

Table 1*Franchise Areas of MWSI and MWCI*

MWSI	MWCI
West Zone Service Area <ul style="list-style-type: none"> • Cities of Manila (except San Andres and Sta. Ana), Pasay, Parañaque, Caloocan, Muntinlupa, Las Piñas, Valenzuela, Navotas, Malabon, and parts of Makati and Quezon City Province of Cavite <ul style="list-style-type: none"> • Cities of Cavite, Bacoor and Imus • Municipalities of Kawit, Noveleta, and Rosario 	East Zone Service Area <ul style="list-style-type: none"> • Cities of Makati, Mandaluyong, Pasig, San Juan, Taguig, Marikina, and parts of Quezon City and Manila • Municipality of Pateros Province of Rizal <ul style="list-style-type: none"> • Antipolo City • Municipalities of Angono, Baras, Binangonan, Cainta, Cardona, Jala-Jala, Morong, Pililia, Rodriguez, Tanay, Taytay, Teresa, and San Mateo

Note. Section 2(b) of RAs 11600 and 11601

Under the Revised Concessionaire Agreement of the MWSI and MWCI, the MWSS hereby grants to the Concessionaires, as public utilities, to perform certain functions and as public utilities for the exercise of certain rights and powers under the MWSS Charter, the right to manage, operate, repair, decommission and refurbish the Facilities in the Service Area, including the right to bill and collect for water and sewerage services supplied in the Service Area. The following are the rights and obligations assigned by the MWSS under its Charter to the Concessionaires solely in relation to the Service Area:

- a. Finance, design, and construct the Facilities, except as otherwise provided in the Concessionaire Agreement;
- b. Undertake the operation and maintenance of the Facilities in the Service Area;
- c. Treat raw water and wastewater in the Service Area;
- d. Provide and manage the services to the Customers;
- e. Bill and collect payment from the Customers for the services;
- f. Source raw water from catchment areas, watersheds, springs, wells, and reservoirs in the Service Area, subject to the applicable Authorizations from the relevant Government Authorities; and
- g. Provide connections to public sewer and septic and sanitation cleaning as sewerage services.

In addition, Section 3 of RAs 11600 and 11601 provides for the following rights and privileges to the MWSI and MWCI:

- a. Develop, finance, construct, install, maintain, operate, as its operation may require, water sources, including new raw water sources, including deep wells, dams, aqueducts, tunnels, treatment plants, reservoirs, pump stations, and facilities for the transmission, conveyance, and distribution of water including pipelines, machineries, and other waterworks for the purpose of supplying water in the Franchise Area, for domestic, commercial, industrial, and other purposes;
- b. Recover, supply, distribute, and reuse treated and grey water, whether in bulk or retail, within the Franchise Area for domestic, commercial, or industrial, and other purposes;
- c. Finance, construct, install, maintain, and operate sewerage systems, whether separate or combined, as may be necessary for the proper sanitation and other uses within the Franchise Area: Provided, That the grantee may only offer services to non-residential customers for industrial effluents compatible with available treatment processes;
- d. Purify water from deep well, reservoirs, dams, and other water sources subject to the approval of the Department of Health or any other government agency concerned;
- e. Construct works across, over, through, or alongside any stream, water-course, canal, ditch, public places, bridge, street, avenue, highway, or railway, as the location of said works may require: Provided, That the works be constructed in a manner as to afford security to life and property, and to the extent reasonably possible not to obstruct traffic: Provided, further, That the stream, water-course, canal, ditch, public places, bridge, street, avenue, highway, or railways so crossed or intersected shall be restored as provided in Section 6 of both laws; and
- f. Disconnect water supply and discontinue provision of water or wastewater services if the customer defaults in the payment of fees for the services provided or for acts of pilferage pursuant to RA 8041⁶ or the “National Water Crisis Act of 1995”.

The Concessionaire Agreements shall expire on July 31, 2037 but they can be extended up to the term of the franchise, which is 25 years from the effectivity of RAs 11600 and 11601 unless sooner canceled or revoked by Congress when the public interest so requires or when the grantees fail to comply with regulatory standards reasonably. It is noted that RA 11600, or the MWSI franchise, took effect on January 22, 2022⁷, which means that the Concessionaire Agreement can be extended up to 2047 or 10 years after its expiration date.

⁶ Entitled, “An Act to Address the National Water Crisis and for Other Purposes”, (June 7, 1995).

⁷ Business World. (2022, January 11). Maynilad’s new franchise takes effect on Jan. 22. <https://www.bworldonline.com/maynilads-new-franchise-takes-effect-on-jan-22/>

With regard to their tax liabilities, Section 23 of both laws provides that MWSI and MWCI shall continue to pay for income taxes, which they cannot pass on to their customers. Likewise, they are liable to the same taxes that similar persons or corporations pay on their real estate buildings and personal property. It is also noted that under Section 6.2 of the Revised Concessionaire Agreements, the MWSI and MWCI shall be responsible for all income and withholding taxes and other forms of taxes arising from payments by customers for services rendered on and after the Commencement Date and from any other income associated with the Concession arising on or after the Commencement Date.

The MWSI and MWCI shall also be responsible for the payment of the following under the Concessionaire Agreement:

- a. All documentary stamp taxes payable in connection with the execution of the Concessionaire Agreement and any related agreements or instruments;
- b. All customs, import duties, and other taxes or assessments relating to the importation into the Philippines of plant and equipment to be used in connection with the Concession; and
- c. All other local transfer taxes on property acquired through the exercise of rights pursuant to Section 7.2 (Easements, Eminent Domain, Right of Way, and Similar Powers) of the Concessionaire Agreement.

The MWSI and MWCI shall also pay for and on behalf of the MWSS or shall reimburse the MWSS within 10 days of the demand therefor, any real property taxes and other taxes or assessments payable by the MWSS on its properties or assets in the Service Area used for the supply of water and sewerage services.

Prior to the passage of RAs 11600 and 11601, water concessionaires were liable to pay the 12% value-added tax (VAT) on their sale of services. Likewise, it is noted that water utilities such as the MWSS and local water districts are subject to the 2% national franchise tax (NFT) on gross receipts derived from the business covered by the law granting the franchise under Section 119 of the NIRC of 1997, as amended. Moreover, Section 109(E) of the NIRC of 1997, as amended, exempts services subject to percentage tax such as franchise tax from the 12% VAT.

In relation to this, the Regulatory Office of the MWSS (MWSS-RO) announced through a press release dated March 3, 2022, that with the passage of RAs 11600 and 11601, the total current charges for water and wastewater services in the customers' Statements of Account (SOA) should no longer be subject to the 12% VAT, but to the 2% NFT, and the actual rate of local franchise tax (LFT) implemented by the local government units within their Franchise Area.⁸

⁸ MWSS-RO. (2022, March 3). Press Release: MWSS RO Announces Reduction in Maynilad and Manila Water Customers' Water Bills. <https://ro.mwss.gov.ph/press-release-mwss-ro-announces-reduction-in-maynilad-and-manila-water-customers-water-bills/>

Although Section 23 of both laws did not explicitly provide for the VAT exemption and imposition of the NFT, since the MWSI and MWCI are now operating under a CPCN, which is in the form of its Concession Agreement with the MWSS, they are now liable to the 2% NFT under Section 119 of the NIRC of 1997, as amended, instead of the 12% VAT. It is noted that public utilities with CPCN are usually subject to other percentage taxes instead of the VAT, such as domestic common carriers.

As a result of the changes from VAT to NFT, a reduction in the MWSI and MWCI customers' monthly water bills are expected (see Figure 1). The OPT and LFT shall be reflected as "Government Tax" in the customers' SOA beginning March 21, 2022. Since MWSI and MWCI are no longer liable to the VAT, both water concessioners with CPCN from the MWSS would decrease the water service rates, however, MWSI and MWCI cannot recover their input VAT on water services and related services. Nevertheless, the decrease in water service rates is in favor of the end-consumer however, it would not be guaranteed that the water service rates will not increase since the input VAT will be a factor on the expense of the MWSI and MWCI and eventually will be passed on to the end-consumer.

Figure 1. Impact of RAs 11600 and 11601 on MWSI and MWCI customers' water bills.
(Source: <https://newsinfo.inquirer.net/files/2022/03/WhatsApp-Image-2022-03-03-at-11.59.24-AM.jpeg>)

IMPACT ON CUSTOMERS' WATER BILLS:					
MAYNILAD					
Monthly Bills	With VAT (12%)	With Govt Tax (2.0%)	Inc. (Dec.)	With Govt Tax (2.825%)	Inc. (Dec.)
10 cu.m.	130.42	118.78	(11.64)	119.74	(10.68)
20 cu.m.	488.82	445.18	(43.64)	448.78	(40.04)
30 cu.m.	997.93	908.83	(89.10)	916.18	(81.75)
MANILA WATER					
Monthly Bills	With VAT (12%)	With Govt Tax (2.5%)	Inc. (Dec.)	With Govt Tax (2.825%)	Inc. (Dec.)
Low income-10 cu.m	86.56	79.22	(7.34)	79.47	(7.09)
10 cu.m.	151.22	138.40	(12.82)	138.83	(12.39)
20 cu.m.	333.47	305.18	(28.29)	306.15	(27.32)
30 cu.m.	679.01	621.42	(57.59)	623.39	(55.62)