

Tax Implications of Republic Act Nos. 11537^{1*}

I. FEATURES

RA 11537 extended for another 25 years from its expiration on April 24, 2023, the franchise granted under RA 8627² to Mindanao Islamic Telephone Company, Inc. (Mislattel), presently known as Dito Telecommunity Corporation (DITO).

The franchise grantee, its successors or assignees, shall have the right, privilege and authority to carry on the business of providing telecommunications services in and between provinces, cities and municipalities in the Philippines and between the Philippines and other countries and territories and, for this purpose, to establish, operate, manage, lease, maintain and purchase telecommunications systems, and other telecommunications systems, fiber optics, satellite transmission and reception systems, and other telecommunications systems and their value-added services such as transmission of voice, data, facsimile, control signs, audio and video, and all other telecommunications systems technologies as are at present available or will be made available through technical advances or innovations in the future, or construct, acquire, lease, and operate or manage transmitting and receiving stations and switching stations, both for local and international services, lines, cables or systems, as is, or are, convenient or essential to efficiently carry out the purpose of the franchise.

The grantee shall secure from the National Telecommunications Commission (NTC) a Certificate of Public Convenience and Necessity (CPCN)³ or the appropriate permits and licenses for the construction, installation, and operation of its telecommunications systems/facilities. The NTC shall have the power to impose such conditions relative to the construction, operation, maintenance, or service level of the telecommunications systems, as

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¹ Entitled, “An Act Renewing for Another Twenty-Five (25) Years the Franchise Granted to Mindanao Islamic Telephone Company, Inc., Presently Known as Dito Telecommunity Corporation, under Republic Act No. 8627, Entitled “An Act Granting the Mindanao Islamic Telephone Company, Inc., a Franchise to Construct, Establish, Install, Maintain and Operate Wire and/or Wireless Telecommunications Systems in the Philippines”, (May 18, 2021).

² Entitled, “An Act Granting the Mindanao Islamic Telephone Company, Inc., A Franchise to Construct, Establish, Install, Maintain and Operate Wire and/or Wireless Telecommunications Systems in the Philippines”, (April 19, 1998).

³ A CPCN or authorization predicted on a valid congressional franchise is required before an entity is allowed to install, operate and maintain public telecommunications facilities and services in the country.

well as the authority to regulate the construction and operation of the grantee's telecommunications systems.

The law requires the grantee to provide mobile number portability (MNP) and its implementing mechanism, including the required infrastructure and processes, and shall directly or indirectly interconnect with the infrastructure, facilities, systems, or equipment of other telecommunications franchise grantees. The grantee shall not install network features, functions, or capabilities that will impede the implementation of a nationwide MNP system.

The law also mandates the franchise grantee to provide and promote the creation of employment opportunities as well as accept on-the-job trainees in their franchise operations. Priority shall be given to the residents of the place where the principal office of the grantee is located, and the grantees shall ensure that at least 60% of its employees are regular employees, and in no case shall the percentage of contractual employees, job orders, casuals, and independent contractors combined, exceed 40% of its total workforce.

Under Section 18 of the law, the grantee, its successors, or assignees shall be liable for the following taxes:

- a. Same taxes on real estate, buildings, and personal property, exclusive of the franchise, as other persons or corporations which are now or hereafter may be required by law to pay;
- b. Value-added tax (VAT) on all gross receipts of the business transacted under its franchise by the grantee, its successors, or assignees, in the Philippines, in lieu of any and all taxes of any kind, nature or description levied, established or collected by an authority whatsoever including, but not limited to, city, municipal, provincial or national, from which the grantee is hereby expressly exempted effective from the date of effectivity of RA 11537; and
- c. Income taxes payable under Title II of the National Internal Revenue Code (NIRC) of 1997, as amended, pursuant to Section 2 of Executive Order No. 72 unless the latter enactment is amended or repealed, in which case the amendment or repeal shall be applicable thereto.

Meanwhile, the radio telecommunications and electronic communications equipment, machinery, and spare parts needed in connection with the grantee's business shall be exempt from customs duties, tariffs, and other taxes.

The grantee 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.

The grantee shall also submit the regular security audits of its network and facilities by the Department of Information and Communications Technology (DICT) and the National Security Council (NSC), among others, to Congress as part of its reportorial requirements.

The law also provided for an equality clause which states that any advantage, favor, privilege, exemption, or immunity granted under other existing franchises, or may hereafter be granted, upon prior review and approval of Congress, shall ipso facto become part of the previously granted telecommunications franchises and shall be accorded immediately and unconditionally to the grantees of such franchises: Provided, however, That the foregoing shall neither apply to nor affect the provisions of telecommunications franchises concerning territory covered by the franchise, the life span of the franchise, or the type of service authorized by the franchise.

II. BACKGROUND INFORMATION

RA 11537 granted DITO a new franchise less than two years before its old franchise under the name Mislattel will expire on April 24, 2023. The DITO is a consortium of Davao businessman Dennis Uy's Udenna Corporation and its subsidiary Chelsea Logistics Corporation and Chinese state-owned China Telecommunications Corporation, a parent company of China Telecommunications Corporation (Chinatel).

The Udenna Corporation and its subsidiary Chelsea Logistics Corporation had formalized the investment agreement with Chinatel that would develop and operate the third telecommunications service provider in the country. Under the investment agreement, Chinatel committed to investing P279 billion in the franchise of Mislattel.⁴ The share-purchase agreement that would realize the operation of the third telecommunications player was signed on June 13, 2019.⁵

The DITO was commercially launched on March 18, 2021 in 15 selected cities in Cebu and Davao and included 21 more cities on April 16, 2021. As of February 2022, DITO has connected more than 6 million subscribers nationwide in over 500 DITO-covered areas, nearing 5,000 towers erected, more than 22 kilometers of fiber optic cables, above 42,000 retail partners, and 16 DITO experience stores placed strategically in Luzon, Visayas, and Mindanao.

As part of its commitment to the government to help improve telecommunications services in the Philippines, DITO offers mobile number portability (MNP) in compliance with RA 11202⁶ (Mobile Number Portability Act). The MNP is a global practice that enables mobile phone customers to keep their number even when they switch networks or change their subscription from postpaid to prepaid and vice versa, free of charge. Under the MNP Act,

⁴ Chelsea. (2019, April 26). Udenna & Chinatel Ink US\$5.4 B Investment to Promote World-Class Telecommunications Service. Press Release. https://www.chelsealogistics.ph/wp-content/uploads/2019/05/PR-CLC-April-26-2019_vF-Mislattel.pdf

⁵ Chelsea. (2019, June). Udenna, Chelsea, and China Telecom sign SPA to obtain 'permit to operate' in July. Press Release. <https://www.chelsealogistics.ph/wp-content/uploads/2019/06/PR-Mislattel-Consortium-Signs-SPA-06-14-2019.pdf>

⁶ Entitled, "An Act Requiring Mobile Service Providers to Provide Nationwide Mobile Number Portability to Subscribers", (February 8, 2019).

switching from different telecommunications providers is expected to be successful within 48 hours after the request, with no conditions or procedures imposed.

To enable the porting services for the MNP Act and ensure its smooth implementation, all three Philippine telecommunications companies (Globe, SMART, and DITO) formed an alliance through Telecommunications Connectivity Inc. (TCI), which will oversee all the activities under the MNP. While the MNP Act was enacted on February 8, 2019, its implementation was delayed and started only in September 2021 due to the COVID-19 pandemic.

III. IMPLICATIONS

According to the DICT, the entry of DITO as the third telecommunications player would improve internet connectivity and strengthen the digital infrastructure and connectivity in the country. DITO received its first CPCN from the NTC in July 2019. As indicated in the CPCN, DITO committed to provide 37.03% of the national population with a minimum average broadband speed of 27 megabits per second (Mbps).⁷

R.G. Manabat & Co. was the independent technical auditor that assessed whether or not the DITO fulfilled its commitments under the CPCN. According to the findings submitted to the NTC, DITO satisfied and exceeded its commitment at 37.48%, equivalent to 37,845,315 of the national population, and covered 8,860 barangays. Initially, the roll-out area services offered by DITO included areas in Metro Cebu and Metro Davao. It was also reported that DITO's minimum average broadband speed was 85.9 Mbps (4G) and 507.5 Mbps (5G).⁸ Based on the 2021 report conducted by Ookla⁹, the Philippines moved up in the global mobile internet speed rankings from the 111th spot to the 86th spot, with the speed test showing a 4.10% increase from 31.44 Mbps for fixed broadband and 14.53% from 22.50 Mbps for mobile.¹⁰

Moreover, under its franchise law, DITO must submit regular reports and security audits of its network and operations to the DICT and the NSC to safeguard the country's national interest and avoid political maneuvering from any foreign government.

With regard to the equality clause under Section 21 of RA 11537, the word "exemption" refers to the exemption from certain grants under existing franchises but does not include any tax exemptions. The interpretation was settled in the case of the Philippine Long Distance

⁷ DICT. (2021, March 9). DICT expects development in PH internet with third telco's commercial launch. <https://dict.gov.ph/dict-expects-devt-in-ph-internet-with-third-telcos-commercial-launch/#:~:text=DITO%20Telecommunity%20received%20its%20CPCN,as%20the%20third%20major%20telco.>

⁸ Ibid.

⁹ Ookla is part of Ziff Davis, a vertically focused digital media and internet company whose portfolio includes leading brands in technology, entertainment, shopping, health, cybersecurity, and martech. Ookla's headquarters is located in Seattle, WA, USA with additional offices around the world. (<https://www.ookla.com/about>)

¹⁰ Ibid.

Telephone Company, Inc. vs. the City of Davao.¹¹ The Supreme Court ruled that RA 7925¹², also known as the Public Telecommunications Policy Act of the Philippines, is a legislative enactment designed to set the national policy on telecommunications and provide the structures to implement it to keep up with the technological advances in the industry and the needs of the public. The thrust of the law is to gradually promote the deregulation of the entry, pricing, and operations of all public telecommunication entities and, thus, promote a level playing field in the telecommunications industry. There is nothing in the language of Section 23 nor in the proceedings of both the House of Representatives and the Senate in enacting RA 7925 which shows that it contemplates the grant of tax exemptions to all telecommunications entities, including those whose exemptions had been withdrawn by the Local Government Code (LGC) of 1991, as amended.

The Court further explained that the word “exemption” in Section 23 of RA 7925 could only contemplate the exemption from certain regulatory or reporting requirements, bearing in mind the policy of the law. Hence, the equality treatment in the franchise cannot be used as the basis for tax exemption.

At present, telecommunications companies are subject to the corporate income tax, VAT, overseas communication tax under the NIRC of 1997, as amended, and to the real property tax and local franchise tax under RA 7160¹³, also known as “the LGC of 1991”, as amended. Hence, DITO shall also be liable for the same taxes as any other telecommunications company. However, radio telecommunications and electronic communications equipment, machinery, and spare parts needed in connection with the business of DITO shall be exempt from customs duties, tariffs, and other taxes under RA 11537. The said exemption on such equipment would boost DITO to install and establish telecommunications towers and support connectivity throughout the country, resulting in better services and competition with other telecommunications service providers.

¹¹ G.R. No. 143867. (2003, March 25). Philippine Long-Distance Telephone Company, Inc., *petitioner* vs. City of Davao and Adelaida B. Barcelona, in her Capacity as the City Treasurer of Davao, respondents. <https://nlpdl.nlp.gov.ph/SC01/2003mar/143867.htm>

¹² Entitled, “An Act to Promote and Govern the Development of Philippines Telecommunications and the Delivery of Public Telecommunications Services”, (March 1, 1995).

¹³ Entitled, “An Act Providing for a Local Government Code of 1991”, (October 10, 1991).