THE PHILIPPINES

TRADE SUMMARY

U.S. goods exports in 2013 were $8.4 billion, up 4.2 percent from the previous year. Corresponding U.S. imports from Philippines were $9.3 billion, down 3.3 percent. The U.S. goods trade deficit with Philippines was $862 million in 2013, down $658 million from 2012. Philippines is currently the 34th largest export market for U.S. goods.

U.S. exports of private commercial services (*i.e.*, excluding military and government) to Philippines were $2.5 billion in 2012 (latest data available), and U.S. imports were $3.7 billion. Sales of services in Philippines by majority U.S.-owned affiliates were $3.6 billion in 2011 (latest data available), while sales of services in the United States by majority Philippines-owned firms were $35 million.

The stock of U.S. foreign direct investment (FDI) in Philippines was $4.6 billion in 2012 (latest data available), down from $4.8 billion in 2011. U.S. FDI in the Philippines is mostly in the manufacturing sector.

IMPORT POLICIES

Tariffs

The Philippines' simple average most favored nation (MFN) tariff is 6.1 percent. Five percent of applied tariffs are 20 percent or higher. All agricultural tariffs and about 60 percent of non-agricultural tariff lines are bound in the WTO, *i.e.*, the Philippines cannot raise tariff rates above this level without offering tariff compensation. The simple average bound tariff in the Philippines is 25.7 percent. Products with unbound tariffs include certain automobiles, chemicals, plastics, vegetable textile fibers, footwear, headgear, fish, and paper products. Applied tariffs on fresh fruit including grapes, apples, oranges, lemons, grapefruits, and strawberries are between 7 percent and 15 percent, whereas bound rates are much higher at 40 percent and 45 percent.

High in-quota tariffs for agricultural products under the Philippines' tariff-rate quota program, known locally as the Minimum Access Volume (MAV) system, significantly inhibit U.S. exports to the Philippines. Under the MAV system, the Philippines imposes a tariff rate quota on numerous agricultural products, including corn, coffee/coffee extracts, potatoes, pork, and poultry products. In-quota tariffs range from 30 percent to 50 percent. Sugar has the highest in-quota tariff at 50 percent, followed by rice, poultry, and potatoes at 40 percent. The in-quota tariff for corn is 35 percent, while pork and raw coffee have in-quota tariffs of 30 percent. Since 2005, the Philippines has maintained MAV levels at its Uruguay Round commitments despite increasing demand in the Philippine market for MAV products.

Quantitative Restrictions

The National Food Authority (NFA) controls rice imports through quantitative restrictions and provides price support to growers of rice. NFA's stated objectives are to achieve self-sufficiency and to ensure sufficiently high and stable food prices to enhance farm incomes and alleviate rural poverty. According to the WTO, NFA's policies have contributed to the sector's non-competitiveness by reducing incentives for farmers to minimize production costs and improve efficiency.

The special treatment for rice accorded to the Philippines in Annex 5 of the WTO Agreement on Agriculture, under which the Philippines maintains a rice quota of 350,000 metric tons, expired on June

30, 2012. The Philippines is negotiating with other WTO Members, including the United States, to extend its exemption from WTO tariffication obligations through 2017.

Automobile Sector

The Philippines continues to apply high tariffs on finished automobiles and motorcycles, including a 30 percent tariff on passenger cars; tariffs of 20 percent to 30 percent on vehicles for the transport of goods; and tariffs of 15 percent to 20 percent on vehicles for the transport of persons, depending on vehicle weight. ASEAN countries and Japan enjoy preferential import tariffs on new vehicle imports under the ASEAN Free Trade Agreement and the Japan-Philippines Economic Partnership Agreement, respectively. The Philippines continues to extend zero duty treatment on imports of capital equipment, spare parts, and accessories by motor vehicle manufacturers and other enterprises registered with the Board of Investments (BOI).

Motor vehicle production is covered under the Philippine Motor Vehicle Development Program (MVDP). This program, implemented by BOI, is designed to spur exports and encourage local assembly through low tariffs on components. A 1 percent tariff applies to completely knocked-down kits (CKDs) imported by MVDP-registered participants. CKDs of alternative fuel vehicles enter duty free. The policy also prohibits the importation of used motor vehicles.

Manufacture and assembly of motor vehicles, parts, and components is a preferred activity under the 2013 Philippine Investment Priorities Plan (*see Subsidies section below*).

Safeguards

Since 2002, the Department of Agriculture has maintained a price-based special safeguard on imports of chicken, approximately doubling the effective rate of protection for out-of-quota imports. The imposition of the special safeguard reportedly stems from domestic industry pressure for import protection.

Excise Tax on Distilled Spirits

For many years, the Philippines applied excise taxes to distilled spirits that differed depending on the product from which the spirit is distilled. Spirits made from the sap of nipa, coconut, cassava, camote, or buri palm, or from the juice, syrup, or sugar of the cane, which are typically produced domestically, were taxed at a low rate. Under this system, all other spirits including imported spirits were taxed at a higher rate.

In 2010, the United States and European Union brought disputes at the WTO challenging the Philippines tax system on distilled spirits. In 2011, a WTO panel found that the Philippine excise taxes on imported distilled spirits were discriminatory and inconsistent with the Philippines' WTO obligations under Article III:2 of the GATT 1994. The WTO Appellate Body affirmed these findings in December 2011.

On December 20, 2012, President Aquino signed into law a new excise tax system for distilled spirits. It provides for a 20 peso tax, based on a standard size bottle, and an additional *ad valorem* tax of 15 percent by value in the first two years, increasing to 20 percent by value on January 1, 2015. The specific tax of 20 pesos will increase 4 percent per year every year starting January 1, 2016. The United States will carefully monitor implementation of the system to ensure that it does not discriminate against imported products.

Customs Barriers

Reports of corruption and irregularities in customs processing persist, including undue and costly delays (*e.g.*, irregularities in the valuation process, 100 percent inspection and testing of some products, and customs officials seeking the payment of unrecorded facilitation fees). Some exporters report, for instance, that the Philippine Bureau of Customs does not recognize their established prices and instead applies a higher dutiable value based on information from unspecified sources.

GOVERNMENT PROCUREMENT

Government procurement laws and regulations favor Philippine-controlled companies and locally-produced materials and supplies. The Government Procurement Reform Act of 2003 sought to consolidate procurement laws, simplify prequalification procedures, introduce objective and nondiscretionary criteria in the selection process, and establish an electronic single portal for government procurement activities. However, implementation remains inconsistent. U.S. companies have expressed concern about delayed procurement decisions, delayed payment, and different interpretations of the procurement law among Philippine government agencies.

Since 1993, the Philippine government has maintained a countertrade requirement of 50 percent of the price of imports for procurement by government agencies and government-controlled corporations with penalties for nonperformance of countertrade obligations.

The Philippines is not a signatory to the WTO Agreement on Government Procurement.

SUBSIDIES

The Philippines offers a wide array of fiscal incentives for export-oriented investment, particularly investment related to manufacturing. These incentives are available to firms located in export processing zones, free port zones, and other special industrial estates registered with the Philippine Economic Zone Authority. The available incentives include: income tax holidays or exemption from corporate income tax for four years, renewable for a maximum of eight years; after the income-tax-holiday period, payment of a special 5 percent tax on gross income, in lieu of all national and local taxes; exemption from duties and taxes on imported capital equipment, spare parts and supplies, and raw materials; domestic sales allowance of up to 30 percent of total sales; exemption from wharfage dues, imposts, and fees; zero VAT rate on local purchases, including telecommunications, electricity, and water; and exemption from payment of local government fees (*e.g.*, mayor's permit, business permit, health certificate fee, sanitary inspection fee, and garbage fee). Furthermore, under the Omnibus Investment Code, which is administered by the BOI, tax incentives are available to producers of non-traditional exports, including electronics, garments, textiles, and furniture, and for activities that support exporters, such as logistics services and product testing.

The Philippine government offers incentives to Philippine companies for investment in less developed economic areas and in preferred sectors, as outlined in Board of Investment's Investment Priority Plan (IPP). The incentives include: income tax holidays; tax deductions for wages and certain infrastructure investments; tax and duty exemptions for imported breeding stock and genetic materials; and tax credits on local purchases of breeding stock and materials. An enterprise with less than 60 percent Philippine equity may enjoy incentives if its projects are classified as "pioneer" under the IPP. Pioneer status can be granted to Board of Investment-registered enterprises engaged in the production of new products or using new methods, producing goods deemed highly essential to the country's agricultural self-sufficiency program, or producing or utilizing non-conventional fuel sources. Export-oriented firms, defined as exporting at least 70 percent of production, may also qualify for incentives under the IPP.

The Philippines has not filed a subsidy notification under the WTO Agreement on Subsidies and Countervailing Measures since September 1997.

INTELLECTUAL PROPERTY RIGHTS PROTECTION

The Philippines remained on the Special 301 Watch List in 2013. U.S. rights holders report concerns about increasing Internet-based piracy, cable signal piracy, and provisions in the patent law that may preclude the issuance of patents on certain chemical forms unless the applicant demonstrates increased efficacy. The availability of pirated and counterfeit goods in the Philippines and a judiciary lacking adequate experience in enforcing intellectual property rights (IPR) are additional concerns.

Building on previous efforts, the Philippines in 2013 worked to address these issues through amendments to its IP code, including measures on secondary liability and statutory damages, as well as legislation addressing cable signal piracy and IP infringement relating to money laundering. The new measures also granted new administrative IP enforcement powers. Rights holders report improved coordination and effectiveness of its enforcement efforts and that incidents of unauthorized camcording remain relatively few in number.

SERVICES BARRIERS

Telecommunications

Philippine regulators have defined telecommunications services as a public utility, which under the Philippine Constitution limits foreign equity ownership in telecommunications companies to 40 percent. Foreigners may not serve as executives or managers of telecommunications companies, and the number of foreign directors allowed is tied to the proportion of foreign investment in the company. The United States has urged the Philippines to reclassify telecommunications outside of the utility definition, as it has done for electricity generation. Efforts to liberalize the foreign investment regime in the telecommunications sector suffered a further setback in 2013 when the Philippines Security and Exchange Commission, based on a 2011 Philippines Supreme Court ruling, upheld an expansive interpretation of what constituted a utility. This action effectively limited foreign ownership to levels set out in the Philippines GATS schedule.

The Philippines also applies the public utility designation to value-added services, which is particularly burdensome to service suppliers and inconsistent with international practice. Finally, foreign equity in private radio communications is limited to 20 percent, and foreign ownership of cable television and all other forms of broadcasting and media is prohibited.

Insurance

The Philippines permits up to 100 percent foreign ownership in the insurance sector; however, its GATS commitment caps foreign ownership at 51 percent. Minimum capital requirements increase with the degree of foreign equity.

Generally, only the state-owned Government Service Insurance System (GSIS) may provide insurance for government-funded projects. A 1994 order requires sponsors of build-operate-transfer projects and privatized government corporations to secure their insurance and bonding from the GSIS at least to the extent of the government's interest. All reinsurance companies operating in the Philippines must cede to the industry-controlled National Reinsurance Corporation of the Philippines at least 10 percent of outward reinsurance placements.

Banking

The Philippines applies restrictions on foreign participation in the banking sector in two tiers. Those foreign banks that meet specific requirements, such as diversified ownership, public listing in the country of origin, and global or national rankings, are limited to owning 60 percent of the equity in a locally incorporated banking subsidiary. Those banks that do not meet the criteria, as well as non-bank investors, are subject to a 40 percent ownership ceiling.

Under a 1994 law and its implementing regulations, majority Philippine-owned domestic banks must control at least 70 percent of the resources or total assets in the banking system. This requirement acts as a secondary limit on foreign participation in the banking system.

Since 1999, foreign investments are limited to existing banks due to a central bank moratorium on the issuance of new bank licenses. Furthermore, foreign banks allowed in the Philippines market under the 1994 Foreign Bank Liberalization Act cannot open more than six branches. The four foreign banks that operated in the Philippines prior to 1948 may operate up to six additional branches each.

In June 2011, the Philippine Central Bank announced a phased lifting of branching restrictions for locally incorporated commercial and thrift banks in eight key Metro Manila cities. Before branching restrictions in the key cities are fully lifted in July 2014, priority will be given to banks with fewer than 200 branches in the previously-restricted areas. This process will benefit foreign banks with commercial and thrift banking subsidiaries in the Philippines.

Financial institutions must set aside loans for certain preferred sectors. The Agri-Agra Law requires banks to earmark at least 25 percent of their loan portfolios for agricultural credit, with at least 10 percent dedicated to agrarian reform program beneficiaries. Although amendments to the Agri-Agra Law in 2010 widened the scope of eligible credits and investments, the new law also scrapped previously allowed, alternative modes of compliance (*i.e.*, financing of educational institutions, hospitals and other medical services, low cost housing, and cooperatives). In addition, the Magna Carta for Micro, Small, and Medium Enterprises requires banks to set aside at least 10 percent of their loan portfolios for these borrowers. These mandatory lending provisions are more burdensome on foreign banks for a number of reasons, including constrained branch networks and foreign land ownership restrictions that impede their ability to enforce rights over land accepted as collateral.

Other Financial Services

For mutual funds, all members of the board of directors must be Philippine citizens, although no foreign ownership restrictions apply. Current laws limit foreign ownership of financing and of securities underwriting companies to 60 percent of voting stock.

The 2007 Lending Company Regulation Act requires majority Philippine ownership for credit enterprises not clearly under the scope of other laws.

Advertising

The Philippine Constitution limits foreign ownership of advertising agencies to 30 percent. All executive and managing officers must be Philippine citizens.

Public Utilities

The Philippine Constitution limits foreign investment in the operation and management of public utilities to 40 percent. Philippine law defines public utility to include a range of sectors including water and sewage treatment, electricity transmission and distribution (although not electricity generation), telecommunications, and transport. All executive and managing officers of public utility companies must be Philippine citizens, and foreign investors may serve on governing bodies only in proportion to their equity.

Professional Services

The Philippine Constitution limits licensing for the practice of professions to Philippine citizens. Under Philippine law, the practice of professions is defined to include law, medicine, nursing, accountancy, engineering, architecture, and customs brokerage.

Express Delivery Services

Foreign equity participation in the domestic express delivery services sector is limited to 40 percent.

Retail Trade

Philippine law restricts foreign investment in small retail ventures to Philippine nationals. Foreigners may own larger retail ventures subject to several requirements, including paid-up capital of $2.5 million or more, an $830,000 minimum investment per store, and parent company net worth of over $200 million. In addition, the retailer must either own at least five retail stores elsewhere or have at least one outlet with capitalization of $25 million or more. For retailers of high-end or luxury products, the minimum investment in each retail store is $250,000 and the net worth of the parent company must exceed $50 million.

Foreign retailers are prohibited from engaging in trade outside their accredited stores, such as through the use of carts, sales representatives, or door-to-door selling. Retail enterprises with foreign ownership exceeding 80 percent of equity must offer at least 30 percent of their shares to local investors within eight years of the start of operations through public offering of stock.

Civil Aviation

The Philippine government applies the Common Carrier Tax and Gross Philippine Billing Tax on cargo traffic carried by non-Filipino airlines. In March 2013 the government amended its internal revenue code to exempt airlines from these taxes for passenger traffic.

INVESTMENT BARRIERS

Significant restrictions apply to foreign investment in the Philippines. The Foreign Investment Negative List (FINL) enumerates foreign investment restrictions in two parts; List A details restrictions mandated by the Constitution or in specific laws, while List B lists restrictions mandated for reasons of national security, defense, public health and morals, and protection of small and medium sized enterprises (SMEs). Foreign investment in sectors enumerated in the FINL may be prohibited outright (*e.g.*, mass media, practice of professions, small-scale mining) or subject to limitation (*e.g.*, natural resource extraction, investment in SMEs). The list is updated every two years, most recently in October 2012. In May 2013, the SEC issued guidelines to monitor corporations for compliance with the foreign equity restrictions mandated by the FINL.

The Philippine Constitution prohibits foreigners from owning land in the country but allows for 50 year leases (with one 25 year renewal). An ambiguous deed and property system can make it difficult to establish clear ownership of leased land, however, and an inefficient judiciary results in land disputes that can extend indefinitely. U.S. investors report that these disputes can be a particularly significant barrier to investment in the mineral exploration and processing sectors.

Trade Related Investment Measures

The Board of Investment imposes a higher export performance requirement on foreign-owned enterprises (70 percent of production) than on Philippine-owned companies (50 percent of production). U.S. stakeholders have also reported that the Philippine government imposes unwritten “trade balancing” requirements on firms applying for approval of ventures under the ASEAN Industrial Cooperation scheme.

OTHER BARRIERS

Corruption remains a pervasive and longstanding problem in the Philippines. Both foreign and domestic investors have expressed concern about the propensity of Philippine courts and regulators to stray beyond matters of legal interpretation into policymaking and about the lack of transparency in judicial and regulatory processes. Concerns also have been raised about courts being influenced by bribery and improperly issuing temporary restraining orders to impede legitimate commerce.