



Republic of the Philippines
DEPARTMENT OF FINANCE

Roxas Boulevard Corner Pablo Ocampo, Sr. Street
Manila 1004

DOF OPINION No. 005.2022

RHEENA LIZA D. DE GUZMAN

Vice President and Treasurer

SAN ROQUE POWER CORPORATION

Makati Administrative Office

The Enterprise Center, Tower 1, 36th Floor,
6766 Ayala Avenue, Makati City, 1200

**SUBJECT: Request for Review of Bureau of Internal Revenue
International Tax Affairs Division (BIR-ITAD) Ruling No. 036-
2021 dated 9 July 2021**

Dear Ms. De Guzman:

This refers to the Request for Review dated 24 September 2021¹ filed by San Roque Power Corporation (SRPC) on behalf of Kansai Electric Power Company, Incorporated (KEPCI), of Bureau of Internal Revenue International Tax Affairs Division (BIR-ITAD) Ruling No. ITAD 036-21 dated 9 July 2021, which ruled that KEPCI is deemed to have a permanent establishment in the Philippines since KEPCI has consistently furnished consultancy services in the Philippines through its employees for more than six (6) months or 180 days in any twelve-month (12-month) period beginning 2012.

As such, the BIR ruled that all service fees paid by SRPC to KEPCI beginning 2012 for the provision of KEPCI's consultancy services in the Philippines in relation to the operation and maintenance of the San Roque Multipurpose Power Facility (Power Facility)² are subject to income tax, pursuant to paragraph 1, Article 7 of the Convention between the Republic of the Philippines and Japan for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income (PH-Japan Tax Treaty), as amended.³

¹ Certified true copy of the annexes to the Request for Review were received on 10 March 2022.

² The San Roque Multipurpose Power Facility is a combined flood control and power generation project (a dam and hydroelectric plant per *page 1 of the BIR ITAD Ruling No.036-2021*) on a build-operate-transfer basis to be located on the island of Luzon, at the lower Agno River in Pangasinan Province, Philippines. Amended and Restated Operation and Maintenance Consulting Agreement dated 30 January 2004, *page 1060 of the docket*.

³ Protocol Amending the PH-Japan Tax Treaty. Date of entry into force: December 5, 2008. Date of effectivity of income covered by the Protocol: January 1, 2009.

SRPC is a corporation duly organized and existing under and by virtue of Philippine laws, while KEPCI is a non-resident foreign corporation organized and existing under the laws of Japan. KEPCI, through its predecessor-in-interest,⁴ entered into an Operation & Maintenance Consulting Agreement (Service Agreement) with KEPCI to assist SRPC on SRPC's operations and maintenance of the Power Facility.

KEPCI agreed to provide SRPC with consultancy services that are necessary for SRPC and its personnel to perform safe, economical and efficient operations, maintenance and repair of the Power Facility. KEPCI dispatched workers to the Philippines to render appropriate services for implementing overall management plans for operations, maintenance, and Power Facility inspections.

On 4 December 2014, SRPC and KEPCI, through Sycip Gorres Velayo and Co. (SGV), filed for tax treaty relief application (TTRA) with the BIR, requesting confirmation that the service fees paid by SRPC to KEPCI are exempt from income tax, as KEPCI does not have a permanent establishment in the Philippines, pursuant to Paragraph 1, Article 7, in relation to Paragraphs 1, 2, and 6, Article 5 of the PH-Japan Tax Treaty, as amended, which provides:

Article 7

1. The profits of an enterprise of a Contracting State shall be taxable only in that Contracting State unless the enterprise carries on business in the other Contracting State through a permanent establishment situated therein. If the enterprise carries on business as aforesaid, the profits of the enterprise may be taxed in that other Contracting State but only so much of them as is attributable to that permanent establishment.

Article 5

1. For the purposes of this Convention, the term "permanent establishment" means a fixed place of business through which the business of an enterprise is wholly or partly carried on.

2. The term "permanent establishment" includes especially: a) a store or other sales outlet; b) a branch; c) an office; d) a factory; e) a workshop; f) a

⁴ On 27 October 1998, SRPC entered into the Service Agreement with Sithe Hong Kong Power Services Ltd. (SHKPS), a company incorporated under the laws of Hong Kong.

On 30 January 2004, Kansai Power International Corporation (KPIC) (a corporation validly existing under the laws of Japan, assumed the obligations and responsibilities of SHKPS under the Service Agreement pursuant to the Assignment, Assumption and Release Agreement among SRPC, SHKPS, and KPIC.

On 1 April 2011, the Service Agreement was further amended following the merger between KPIC and KEPCI effective 31 March 2011. Pursuant to the Amended Service Agreement, KEPCI assumed all KPIC's rights and obligations.

warehouse; g) a mine, an oil or gas well, a quarry or other place of extraction of natural resources.

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6. An enterprise of a Contracting State shall be deemed to have a permanent establishment in the other Contracting State if it furnishes in that other Contracting State **consultancy services, or supervisory services** in connection with a contract for a building, construction or installation project through employees or other personnel – other than an agent of an independent status to whom paragraph 7 applies –, **provided that such activities continue (for the same project or two or more connected projects) for a period or periods aggregating more than six months within any twelve-month period.** However, if the furnishing of such services is effected under an agreement between the Governments of the two Contracting States regarding economic or technical cooperation, that enterprise shall, notwithstanding any provisions of this Article, not be deemed to have a permanent establishment in that other Contracting State.”⁵ (*emphasis supplied*)

In support of their TTRA, SRPC and KEPCI maintained that no permanent establishment is created in the Philippines as the stay of the dispatched KEPCI personnel does not exceed a period aggregating more than six (6) months in any twelve-month (12-month) period. KEPCI submitted an authenticated Certification⁶ issued by KEPCI’s general manager, Toshihiro Takano, providing that the total duration of stay in the Philippines of KEPCI’s personnel for 2011 is only forty five (45) days. As such, there is no contest that KEPCI did not establish a permanent presence in the Philippines for 2011.

However, the BIR ruled that beginning 2012, KEPCI consistently furnished consultancy services in the Philippines through its employees for more than six months or 180 days⁷ in any 12-month period, and being a non-resident corporation, is subject to income tax at the rate of 30% under Section 28(B)(1) of the National Internal Revenue Code (Tax Code), as amended.

⁵ Protocol Amending the Convention Between the Republic of the Philippines and Japan for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income. Date of entry into force: December 5, 2008. Date of effectivity of income covered by the Protocol: January 1, 2009.

⁶ Attached as Annex D in the Request for Review; *pages 1114-1116* of the docket.

⁷ It shall be understood that month is of thirty days, as such, six months is equivalent to 180 days. Article 13, Civil Code of the Philippines (Republic Act No. 386).

The BIR based its findings on its tabulation of the arrival and departure dates stamped on the respective passports submitted by the consultants, summarizing the number of days the dispatched consultants were physically present⁸ in the Philippines, as follows:

2012			
Employees	Arrival	Departure	Days of Physical Presence in the Philippines
Takaki Ishii	February 17, 2012	February 28, 2012	12
Hidehiko Sugimoto	March 11, 2012	March 13, 2012	3
Masato Matsuda	April 24, 2012	April 27, 2012	4
Masato Matsuda	May 27, 2012	June 8, 2012	13
Kenichi Deguchi			
Takeshi Higashijima			
Hidehiko Sugimoto	June 27, 2012	June 30, 2012	4
Takeshi Higashijima	July 26, 2012	October 25, 2012	92
	October 20, 2012	November 11, 2012	13
	November 20, 2012	December 29, 2012	40
Total			181

2013			
Employees	Arrival	Departure	Days of Physical Presence in the Philippines
Takeshi Higashijima	January 7, 2013	July 20, 2013	195
	July 28, 2013	October 5, 2013	70
	October 11, 2013	December 31, 2013	82
Total			347

2014			
Employees	Arrival	Departure	Days of Physical Presence in the Philippines
Hidehiko Sugimoto	January 21, 2014	January 23, 2014	1
Takeshi Higashijima	January 1, 2014	January 22, 2014	22
	March 12, 2014	March 13, 2014	2

⁸ In accordance with the "days of physical presence" method. "Under this method the following days are included in the calculation: part of a day, day of arrival, day of departure and all other days spent inside the State of activity such as Saturdays and Sundays, national holidays, holidays before, during and after the activity, short breaks (training, strikes, lock-out, delays in supplies), days of sickness (unless they prevent the individual from leaving and he would have otherwise qualified for the exemption) and death or sickness in the family." Paragraph 5, Article 15. Commentaries of the Organisation for Economic Cooperation and Development (OECD) Committee on Fiscal Affairs (OECD Commentaries). OECD (2019), Model Tax Convention on Income and Capital 2017 (Full Version),

	March 15, 2014	August 6, 2014	145
Ikeno Yasutomo	August 7, 2014	September 13, 2014	38
	September 20, 2014	December 21, 2014	93
Total			301

2015			
Employees	Arrival	Departure	Days of Physical Presence in the Philippines
Ikeno Yasutomo	January 7, 2015	August 7, 2015	213
	August 21, 2015	August 31, 2015	11
	September 4, 2015	October 3, 2015	30
	October 30, 2015	November 10, 2015	12
	November 13, 2015	December 21, 2015	39
Akira Kawata	December 22, 2015	December 30, 2015	9
Total			314

2016			
Employees	Arrival	Departure	Days of Physical Presence in the Philippines
Ikeno Yasutomo	January 8, 2016	January 13, 2016	6
	January 17, 2016	March 1, 2016	45
	April 1, 2016	June 4, 2016	65
	June 1, 2016	August 8, 2016	60
	August 19, 2016	August 31, 2016	13
	September 26, 2016	October 20, 2016	25
	November 20, 2016	December 21, 2016	32
Araki Hiroyuki	March 21, 2016	March 22, 2016	2
Masumi Kasahara	September 5, 2016	September 8, 2016	4
Hidehiko Sugimoto	September 22, 2016	September 25, 2016	4
Toru Nishikawa	November 14, 2016	November 18, 2016	5
Hidehiko Sugimoto			
Shunsuke Hibi			
Yuichi Yamane			
Araki Hiroyuki	November 16, 2016	November 19, 2016	1
Total			262

2017			
Employees	Arrival	Departure	Days of Physical Present in the Philippines
Ikeno Yasutomo	January 5, 2017	February 2, 2017	29
	October 14, 2017	October 19, 2017	6
Takaki Ishii	February 12, 2017	August 30, 2017	200

	September 8, 2017	October 9, 2017	32
	December 14, 2017	December 31, 2017	18
Yutaka Yamakawa	November 18, 2017	November 24, 2017	7
Total			292

2018			
Employees	Arrival	Departure	Days of Physical Present in the Philippines
Takaki Ishii	January 1, 2018	February 16, 2018	47
	February 19, 2018	August 29, 2018	192
	September 8, 2018	September 8, 2018	1
	September 19, 2018	December 27, 2018	100
Total			340

Accordingly, based on the above summary, the BIR ruled that (1) Takeshi Higashijima, (2) Ikeno Yasutomo, and (3) Takaki Ishii, performed services in the Philippines for more than 183 days in 2013, 2015, 2016, 2017, and 2018. As such, these personnel, being nonresident alien individuals not engaged in trade or business in the Philippines, are subject to income tax at the rate of 25% on their gross income under Section 25(B) of the Tax Code.

KEPCI, however, maintains it did not establish a permanent presence in the Philippines; that for a certain period, some of the personnel mentioned in BIR's summary, (1) Takeshi Higashijima, (2) Ikeno Yasutomo, and (3) Takaki Ishii, should not be included for purposes of determining KEPCI's presence in the Philippines – since for such time, these individuals were no longer considered as KEPCI representatives. KEPCI alleges that these aforesaid individuals were instead deemed employees of SRPC, having been seconded to SRPC. Hence, KEPCI maintains that for such secondment period, they are considered resident alien individuals subject to income tax under Section 24(A)(2) of the Tax Code.

We agree with KEPCI.

KEPCI claims that SRPC employed some of the consultants after the latter's consultancy work with KEPCI, hence, these individuals stopped being representatives of KEPCI. Their presence in the country during such time should therefore not be considered for purposes of determining the period by which KEPCI rendered consultancy services in the Philippines.

In support of this claim, KEPCI submitted certified true copy of the Secondment Agreements and Memoranda for Secondment Agreement.⁹ Under the Secondment Agreement, the seconded employees shall perform certain operations and maintenance functions¹⁰ with respect to the Power Facility. By virtue of said Agreements, the seconded Japanese personnel are deemed employees of SRPC for the periods summarized as follows:

Name of Seconded Employees	Secondment Period
Takeshi Higashijima	July 26, 2012 – March 31, 2013
	April 1, 2013 – March 31, 2014
	April 1, 2014 – July 20, 2014
Ikeno Yasutomo	July 21, 2014 – March 31, 2015
	April 1, 2015 – March 31, 2016
	April 1, 2016 – February 6, 2017
Takaki Ishii	February 7, 2017 – March 31, 2018
	April 1, 2018 – March 31, 2019

In determining the nature of the relationship between SRPC and the seconded employees, this Office finds helpful the following statements in the commentaries of the Organisation for Economic Cooperation and Development (OECD) Committee on Fiscal Affairs (OECD Commentaries), in relation to Article 5 on permanent establishments, and Article 15 concerning income from employment, to wit:

Commentary on Article 5:

39. There are different ways in which an enterprise may carry on its business. In most cases, the business of an enterprise is carried on by the entrepreneur or persons who are in a paid-employment relationship with the enterprise (personnel). This personnel includes employees and other persons receiving instructions from the enterprise (e.g. dependent agents). xxx As explained in 8.11 of the Commentary on Article 15, however, there may be cases where individuals who are formally employed by an enterprise will actually be carrying on the business of another enterprise and where, therefore, the first enterprise should not be considered to be carrying on its own business at the location where these individuals will perform that work. Within a multinational group, it is relatively common for employees of one company to be temporarily seconded to another company of the group and to perform business activities that clearly belong to the business of that other company. xxx The analysis in paragraphs 8.13 to 8.15 of the Commentary on Article 15 will be relevant for the purpose of distinguishing these cases from other cases

⁹ Annex E, G, and I of the Request for Review.

¹⁰ Page 1 of the Secondment Agreement.

where employees of a foreign enterprise perform the enterprise's own business activities.

Commentary on Article 15:

8.4. In many States, however, various legislative or jurisprudential rules and criteria (e.g. substance over form) have been deployed for the purpose of distinguishing cases where services rendered in an employment relationship (contract OF service) from cases where such services should be considered to be rendered under a contract for the provision of services between two separate enterprises (contract FOR services). xxx Subject to the limit described in paragraph 8.11 and unless the context of a particular convention requires otherwise, it is a matter of domestic law of the State of source to determine whether services rendered by an individual in that State are provided in an employment relationship and that determination will govern how that State applies the Convention.

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8.11 xxx The relief provided under paragraph 2 of Article 15 would be rendered meaningless if States were allowed to deem services to constitute employment services in cases where there is clearly no employment relationship or to deny the quality of employer to an enterprise carried on by a non-resident where it is clear that the enterprise provides services, through its own personnel, to an enterprise carried on by a resident. Conversely, where services rendered by an individual may properly be regarded by a State as rendered in an employment relationship rather than as under a contract for services concluded between two enterprises, that State should logically also consider that the individual is not carrying on the business of the enterprise that constitutes the individual's formal employer; this could be relevant, for example, for purposes of determining whether that enterprise has a permanent establishment at the place where the individual performs his activities.

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8.13 The nature of the services rendered by the individual will be an important factor since it is logical to assume that an employee provides services which are an integral part of the business activities carried on by his employer. It will therefore be important to determine whether the services rendered by the individual constitute an integral part of the business of the enterprise to which these services are provided. For that purpose, a key consideration will be which enterprise bears the responsibility or risk for the results produced by the individual's work. xxx

8.14 Where a comparison of the nature of the services rendered by the individual with the business activities carried on by his formal employer and by the enterprise to which the services are provided points to an employment relationship that is different from the formal contractual relationship, the following additional factors may be relevant to determine whether this is really the case:

- who has the authority to instruct the individual regarding the manner in which the work has to be performed;
- who controls and has responsibility for the place at which the work is performed;
- the remuneration of the individual is directly charged by the formal employer to the enterprise to which the services are provided;
- who puts the tools and materials necessary for the work at the individual's disposal;
- who determines the number and qualifications of the individuals performing the work;
- who has the right to select the individual who will perform the work and to terminate the contractual arrangements entered into with that individual for that purpose;
- who has the right to impose disciplinary sanctions related to the work of that individual;
- who determines the holidays and work schedule of that individual.

8.15 Where an individual who is formally an employee of one enterprise provides services to another enterprise, the financial arrangements made between the two enterprises will clearly be relevant, although not necessarily conclusive, for the purposes of determining whether the remuneration of the individual is directly charged by the formal employer to the enterprise to which the services are provided. xxx It is important to note, however, that the question of whether the remuneration of the individual is directly charged by the formal employer to the enterprise to which the services are provided is only one of the subsidiary factors that are relevant in determining whether services rendered by that individual may properly be regarded by a State as rendered in an employment relationship rather than as under a contract for services concluded between two enterprises.

A perusal of the Secondment Agreement vis-à-vis the OECD Commentaries would reveal that during the secondment period, the seconded individuals were considered employees of SRPC, and did not represent KEPCI.

The Secondment Agreement provides that the seconded employees will be assigned to the operations and maintenance staff in connection with the operations, maintenance and management of the Power Facility within the Philippines, and will have such duties and responsibilities as shall be specified by SRPC from time to time during the term of the secondment. The seconded employees shall be under the direction of the Senior Vice President for Operation and Site Administrator (SVP).¹¹ During the secondment period, the seconded employees will perform all work under the control and supervision of

¹¹ As provided under the Scope of Work, Schedule 1 to the Secondment Agreement. Attached as Annex E, G, and I to the Request for Review.

SRPC and shall not be under the control or supervision of KEPCI. KEPCI shall not be responsible to the SRPC for any services performed by the seconded employees for SRPC during such period.¹²

The Secondment Agreement likewise provides that SRPC shall pay the salary and other compensation to the seconded employees, provide the seconded employees with airfare for transportation, accommodation, and all other expenses and incidentals resulting from the performance of the seconded employees' duties and responsibilities, and withhold and remit applicable Philippine social contributions and taxes.¹³ SRPC, under the Secondment Agreement, may even request KEPCI to replace the seconded employees after making a reasonable, good faith determination that the seconded employees' performance of duties is unsatisfactory or inappropriate. The replacement shall be subject to the SRPC's reasonable approval.¹⁴

In this case, it is clear that the presence of the seconded employees in the Philippines during the secondment period is due to their employment with SRPC, and not of KEPCI's. The control or supervision exercised by SRPC over the work of the seconded employees, the fact that SRPC takes over the responsibility for the work of the employees, and that it bears the cost of the salary and other compensation of the seconded employees for the secondment period, are factors that support the conclusion that the seconded individuals are in an employment relationship with SRPC.¹⁵

In fine, KEPCI satisfactorily proved that the presence in the Philippines of the seconded employees during the secondment period should not be considered in computing the numbers of days which KEPCI rendered consultancy services in the country.

In determining whether KEPCI rendered consultancy services in the Philippines for a period or periods aggregating more than 6 months or 180 days within any 12-month period, we give weight to the notarized Certification submitted by KEPCI, containing the names of the entities engaged by KEPCI to perform services in the Philippines for SRPC and the number of days that they rendered

¹² *Id.* 2.2 Status and Duties of the Seconded Employees of the Secondment Agreement.

¹³ *Id.* 3.1 Secondment Payment, 3.2 Payment, 3.3 Expenses, and 3.4 Taxes.

¹⁴ *Id.* 2.3 Substitution of Seconded Employees.

¹⁵ See *Example 5* under paragraph 8.24 and 8.25 of the OECD Commentaries.

services, with the concurrent dates of their arrival and dates of departure.¹⁶ In sum, the days of stay in the Philippines of KEPCI consultants are as follows:

Calendar Year	Number of Days
2012	23
2013	39
2014	22
2015	35
2016	46
2017	62
2018	36

With which, it is this Office's opinion that KEPCI's provision of consultancy services to SRPC for a period not more than 6 months or 180 days, for 2012 until 2018, did not result with KEPCI having created a permanent establishment in the Philippines.

As KEPCI does not have a permanent establishment in the Philippines, the service fees paid to KEPCI, which are in the nature of business profits, are not subject to Philippine income tax, pursuant to Article 7, in relation to Article 5 of the RP-Japan Tax Treaty. These services, having been rendered in the Philippines, are subject to value-added tax at the rate of 12% under Section 108(A) of the Tax Code, as amended. Pursuant to Section 4.115-2 of Revenue Regulations No. 16-2005, as amended, SRPC duly withheld the VAT due on such services.

Moreover, as settled, Takeshi Higashijima, Ikeno Yasutomo, and Takaki Ishii are considered employees of SRPC during the secondment period. As noted in the Request for Review, KEPCI and SRPC did not request for exemption from income tax for these individuals, as SRPC considered them as their employees and therefore, withheld the appropriate taxes and attached in this Request for Review the Income Tax Returns of the seconded employees.¹⁷ As these individuals are considered as employees of SRPC, they are considered as resident aliens subject to income tax under Section 24(A)(2) of the Tax Code.

¹⁶ Certification executed by Masahiko Umesaki, General Manager of KEPCI, attached as Annex D to the Request for Review. Similar content is provided in the Certification executed Rheena Liza De Guzman, Vice President for Finance and Treasurer of SRPC, pages 1155 to 1160 of the docket.

¹⁷ Attached as Annex K in the Request for Review.

In view of the foregoing, this Office grants the Request for Review. This ruling is being issued on the basis of the foregoing facts as represented. However, if upon investigation, it will be disclosed that the facts are different, then this ruling shall be considered as null and void.

Thank you.



Respectfully yours,



Digitally signed by
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CARLOS G. DOMINGUEZ
Secretary



CC: **CAESAR R. DULAY**
Commissioner, Bureau of Internal Revenue