Mining & Natural Resources

Quisumbing Torres

Primer on the Philippine Minerals Industry

DISCLAIMER
It should be noted that the material in this publication is designed to provide general information only. It is not offered as advice on any particular matter, whether it be legal, procedural or other, and should not be taken as such. The authors expressly disclaim all liability to any person in respect of consequences of anything done or omitted to be done wholly or partly in reliance upon the whole or any part of the contents of this publication. No reader should act or refrain from acting on the basis of any matter contained in it without seeking specific professional advice on the particular facts and circumstances at issue.

TABLE OF CONTENTS

I. MINING LAWS AND OTHER REGULATIONS .1
A. The 1987 Philippine Constitution 1
1. Ownership of Natural Resources 1
2. Ownership of Private Lands 1
B. Mining Act 2
1. Exploration Permit 2
2. Mineral Agreements 2
3. Financial And Technical Assistance Agreement 4
4. Mineral Processing Permits 5
C. Qualifications of Applicants for Mineral Rights 5
1. Mineral Agreements 5
2. Exploration Permits, FTAAs, and Mineral Processing Permits 5
D. Capitalization Requirements 5
E. Indigenous Peoples Rights Act Of 1997 .6
1. Free and Prior Informed Consent 6
2. Rights of Ownership 6
3. Right to Develop Lands and Natural Resources 6
4. Right to Benefits 7

II. INVESTMENT GUARANTEES AND INCENTIVES 7
A. Tax Incentives 8
B. Non-tax Incentives 9

III. TAX REGIME 9
A. Income Tax 9
B. Tax on Dividends 11
C. Excise Tax 12
D. Value-Added Tax 12

IV. ENVIRONMENTAL LAWS 13
A. Environmental Impact Statement System 13
B. Ecological Solid Waste Management Act 13
C. Toxic Substances and Hazardous and Nuclear Wastes Control Act 14
D. Clean Air Act 15
E. Clear Water Act 16
F. Pollution Control Law 16
G. Water Code 16
H. National Environmental User's Fee of 2002 17

The Philippines continues to rank as one of the most highly mineralized countries in the world. In terms of mineral potential, studies show that the Philippines ranks third in gold, fourth in copper, fifth in nickel, and sixth in chromite. The Philippines' total untapped mineral wealth is estimated to be worth more than US$840 billion.[1]

I. MINING LAWS AND OTHER REGULATIONS

The Philippine Constitution of 1987 ("Constitution") and the Philippine Mining Act of 1995 ("Mining Act") govern the exploration, development, processing and utilization of mineral resources in the Philippines. Under the Constitution, the State owns all mineral resources. However, the State may enter into agreements with private contractors for the exploitation of mineral resources. The Mining Act and its Implementing Rules and Regulations ("IRR") define these agreements, delineate the various mining rights recognized in the Philippines and provide the requirements for acquiring these mining rights. Other Philippine laws also govern investments in the Philippine mining industry.

A. The 1987 Philippine Constitution

The Constitution provides that all lands of the public domain, water, minerals, coal, petroleum, and other mineral oils, all forces of potential energy, fisheries, forests or timber, wildlife, flora and other natural resources are owned by the state. The exploration, development and utilization of these natural resources are also under the full control and supervision of the state. However, the state has the option of entering into co-production, joint venture or production-sharing agreements with Philippine citizens or Philippine corporations or associations. At least 60% of the capital of a corporation or association must be owned by Philippine citizens before it can be considered as a Philippine corporation or association.

As an exception to this nationality requirement, the Constitution authorizes the President of the Philippines to enter into agreements with foreign-owned corporations involving either financial or technical assistance, for the large-scale exploration, development and utilization of minerals, petroleum and other mineral oils.

1. Ownership of Natural Resources

The Philippine Constitution adheres to the Regalian Doctrine. Under this doctrine, the State owns all natural resources. If an investor wishes to acquire the right to extract or develop natural resources, he must enter into an agreement with the State.

2. Ownership of Private Lands

Only Filipino citizens and corporations 60% Filipino owned may acquire private lands. Any sale or transfer to a disqualified person is null and void. Foreigners and foreign corporations, though disqualified from acquiring private lands, may enter into agreements for the lease of private lands. Foreign investors may lease private lands which will be used exclusively for investments for a period of up to 50 years, renewable once for a period of 25 years.

[1] Figures provided by the Philippine National Economic Development Authority, 29 June 2004.

B. Mining Act

The Mining Act governs the exploration, development, utilization and processing of all mineral resources, and provides the requirements for the acquisition of mineral rights. The acquisition of mineral rights is a process that begins with the acquisition of an Exploration Permit.

1. Exploration Permit

An Exploration Permit is a grant from the Philippine government that gives the permit holder the right to conduct exploration for all minerals within a specified area. An Exploration Permit is valid for a period of two years and can be renewed for another two years but cannot exceed a total of six years.

The maximum areas that an Exploration Permit can cover are as follows:

- Onshore, in any one province
  - for individuals, 20 blocks or 1,620 hectares; and
  - for partnerships, corporations, cooperatives or associations, 200 blocks or 16,200 hectares.
- Onshore in the entire Philippines
  - for individuals, 40 blocks or 3,240 hectares; and
  - for partnerships, corporations, cooperatives or associations, 400 hectares or 32,400 hectares.
- Offshore, beyond 500 meters from the mean low tide level
  - for individuals, 100 blocks or 8,100 hectares; and
  - for partnerships, corporations, cooperatives or associations, 1,000 blocks or 81,000 hectares.

If results of exploration reveal the presence of mineral deposits economically and technically feasible for mining operations, the holder of the exploration permit may, within the term of the Exploration Permit, file a declaration of mining project feasibility. The approval of the declaration of mining project feasibility shall grant the holder of the exploration permit the exclusive right to a Mineral Agreement or Financial and Technical Assistance Agreement ("FTAA") over the permit area. The permit holder may then apply for a mineral agreement with the Philippine government.

2. Mineral Agreements

The Constitution allows the Philippine government to enter into various agreements with private parties for the exploitation of mineral deposits. These mineral agreements are the following:

- Mineral Production Sharing Agreement;
- Co-Production Agreement; and
- Joint Venture Agreement.

All the foregoing mineral agreements grant to the contractor the exclusive right to conduct mining operations and to extract all mineral resources found in the contract area. The contractor may convert its mineral agreement into any of the

other type of mineral agreement, or an FTAA, subject to the approval of the Secretary of the Department of Environment and Natural Resources ("DENR").

The maximum areas that a mineral agreement can cover are as follows:

- Onshore, in any one province -
  - for individuals, 10 blocks or 810 hectares; and
  - for partnerships, cooperatives, associations or corporations, 100 hundred blocks or 8,100 hectares.
- Onshore, in the entire Philippines -
  - for individuals, 20 blocks or 1,620 hectares; and
  - for partnerships, cooperatives, associations or corporations, 200 blocks or 16,200 hectares.
- Offshore, in the entire Philippines -
  - for individuals, 50 blocks or 4,050 hectares; and
  - for partnerships, cooperatives, associations or corporations, 500 blocks or 40,500 hectares.

Where the contract area covered under a mineral agreement is located within the Exclusive Economic Zone, a larger contract area may be granted to the contractor by the Secretary of the DENR. An Exclusive Economic Zone is the water, sea bottom and subsurface measure from the baseline of the Philippine archipelago up to 200 nautical miles offshore.

a. Mineral Production Sharing Agreement

A Mineral Production Sharing Agreement ("MPSA") is an agreement under which the Philippine government grants to the contractor the exclusive right to conduct mining operations within a contract area. The contractor provides the financing, technology, management and personnel necessary for the implementation of the MPSA. The Philippine government then takes a share in the gross output of the mining operation.

All MPSA applications must be filed with the Regional Office of the Mines and Geosciences Bureau ("MGB") of the DENR where the area applied for is situated. An MPSA application may be assigned or transferred to another party, subject to the approval of the MGB Director or the Director of the Regional Office of the MGB where the area applied for is situated.

Pending the approval of the MPSA application by the DENR Secretary, the MGB Director may, upon the request of the MPSA applicant, issue a Temporary Exploration Permit ("TEP") to the MPSA applicant. The TEP is valid for a period of one year. However, the one-year period of the TEP will be deducted from the exploration period of the MPSA. If the MPSA application is disapproved, the TEP is deemed automatically canceled.

After the DENR Secretary approves the MPSA, it will be forwarded to the MGB for numbering. The MPSA contractor must register the MPSA with the concerned MGB Regional Office within 15 working days from receipt of the notice of approval of the MPSA.

An MPSA is valid for 25 years and is renewable for another term not exceeding 25 years. Upon expiration of the MPSA, the Philippine government may itself, or

through a contractor, operate the mine. The contract for the operation of a mine will be awarded to the highest bidder in a public bidding. However, the original MPSA contractor has the right to equal the highest bid upon reimbursement of all reasonable expenses to the highest bidder.

During the exploration period, the MPSA contractor may totally or partially relinquish the original contract area. After the exploration period, prior to or upon approval of the declaration of mining project feasibility, the MPSA contractor must finally relinquish to the Philippine government any portion of the contact area which will not be necessary for the mining operation and which is not covered under any declaration of mining project feasibility.

After relinquishment, the mining area covered under the MPSA cannot exceed the following:

- for metallic minerals - 5,000 hectares; and
- for nonmetallic minerals - 2,000 hectares.

Under the MPSA the Philippine government is entitled to a share in the gross production of the mining operation. The Philippine government's share is taken in the form of an excise tax on the mineral products extracted under the MPSA. The excise tax is computed as follows:

- on metallic minerals, the excise tax based on the actual market value of the gross output thereof at the time of removal shall be as follows:
  - for copper and other metallic minerals except gold and chromite - 2%
  - for gold and chromite - 2%
- on non-metallic minerals and quarry resources - 2% based on the actual market value of the annual gross output thereof at the time of removal.

b. Co-Production Agreement

A Co-Production Agreement is an agreement between the Philippine government and the contractor under which the Philippine government provides inputs to the mining operations other than the mineral resource.

c. Joint Venture Agreement

A Joint Venture Agreement is an agreement under which the Philippine government and the contractor organize a joint venture company in which both parties have equity. The Philippine government takes a share from equity earnings as well as from the gross output of the mining operation.

3. Financial And Technical Assistance Agreement ("FTAA")

Pursuant to the Constitution, the Mining Act provides that the State may enter into an FTAA with qualified persons for the large-scale exploration, development and utilization of mineral resources. Under the Mining Act, qualified persons for an FTAA include 100% foreign-owned corporations.

The contractor must make a minimum investment for development, construction and utilization of US$50,000,000, or its Philippine Peso equivalent in the case of a Filipino contractor. An FTAA may be entered into for the exploration, development and utilization of gold, copper, nickel, chromite, lead, zinc and other minerals. No FTAAs may be granted with respect to cement raw materials, marble, granite, sand and gravel and construction aggregates.

A decision of the Philippine Supreme Court, *La Bugal - B'laan Tribal Association v. Ramos*, issued on 1 December 2004, upheld the constitutionality of the FTAA. In this landmark case, certain non-government organizations claimed, among others, that the FTAA allows foreign contractors to manage mining operations, in violation of the Constitutional principle that the State owns and controls all natural resources. Rejecting this contention, the Supreme Court declared that "[f]ull control is not anathematic to day-to-day management by the contractor, provided that the State retains the power to direct overall strategy… [The State] need not micro-manage mining operations and day-to-day affairs of the enterprise." The Supreme Court also upheld the provision in the Mining Act allowing companies that are up to 100% foreign-owned to enter into an FTAA with the government.

Highlighting estimates by the Philippines' Economic Planning Secretary that the country's untapped mineral wealth is worth US$840 billion, the Supreme Court emphasized the need to jumpstart the economy through mineral resource development. The decision has been hailed by various sectors as a "go-signal" for foreign investment in mining. The Executive Department continues to be a staunch advocate of responsible mining and has issued an executive order enunciating the government policy to promote mining.

4. Mineral Processing Permits

Under the Mining Act, mineral processing means the milling, beneficiation or upgrading of ores or minerals and rocks or by similar means to convert the same into marketable products. A minerals processing permit shall be valid for a period of five years renewable for like periods but not to exceed a total term of 25 years.

C. Qualifications of Applicants for Mineral Rights

1. Mineral Agreements

The following may apply for mineral agreements:

- Philippine citizens; and
- Corporations, partnerships, associations or cooperatives organized or authorized to engage in mining, provided the entity's capital is not more than 40% foreign-owned.

2. Exploration Permits, FTAAs, and Mineral Processing Permits

Foreign-owned corporations (corporations that have more than 40% foreign ownership) are qualified to apply for exploration permits, FTAAs or mineral processing permits.

D. Capitalization Requirements

Applicants for Exploration Permits, Mineral Agreements and FTAAs must possess technical and financial capability to undertake mineral resources development and must be duly registered in accordance with law. Rules and regulations promulgated by the DENR provide that the mining applicant for an Exploration Permit, Mineral Agreement and FTAA must have a minimum authorized capital stock of Ten Million Philippine Pesos (PhP10,000,000.00) and a minimum paid-up capital of Two Million Five Hundred Thousand Philippine Pesos (PhP2,500.000.00). FTAA applicants must have a minimum authorized capital stock of Four Million US Dollars (US$ 4,000,000.00) or its Philippine Peso equivalent.

E. Indigenous Peoples Rights Act Of 1997

The Indigenous Peoples' Rights Act of 1997 ("IPRA") was approved on 29 October 1997. IPRA grants to indigenous cultural communities or indigenous peoples ("ICCs/IPs") certain preferential rights to their ancestral domains and all resources found therein.

Ancestral domains are defined as areas generally belonging to ICCs/IPs, subject to property rights within ancestral domains already existing or vested upon the effectivity of the IPRA, comprising lands, inland waters, coastal areas, and natural resources, held under a claim of ownership, occupied or possessed by ICCs/IPs by themselves or through their ancestors, communally or individually since time immemorial, continuously to the present, except when interrupted by war, *force majeure* or displacement by force, deceit, stealth, or as a consequence of government projects or any voluntary dealings entered into by the government and private persons, and which are necessary to ensure their economic, social and cultural welfare.

1. Free and Prior Informed Consent

No mineral agreement shall be approved unless there is a prior certification from the National Commission on Indigenous Peoples ("NCIP") that the area does not overlap any ancestral domain or that the prior free and informed written consent has been obtained from the ICC/IP concerned.

This consent normally requires entering into a memorandum of agreement with the ICC/IP concerned, through their Council of Elders. The memorandum of agreement will govern the utilization, extraction and development of natural resources within their ancestral domain. This agreement is subject to a limited term of 25 years, renewable at the option of the ICC/IP for another 25 years.

2. Rights of Ownership

ICCs/IPs have rights of ownership over lands, waters, and natural resources and all improvements made by them at any time within the ancestral domains/lands. These rights shall include, but are not limited to, the right over the fruits, the right to possess, the right to use, right to consume, right to exclude and right to recover ownership, and the rights or interests over land and natural resources.

3. Right to Develop Lands and Natural Resources

Subject to property rights within the ancestral domain already existing and/or vested when the IPRA took effect, ICCs/IPs have the right to control, manage, develop, protect, conserve, and sustainably use:

- land, air, water and minerals;
- plants, animals and other organisms;
- collecting, fishing and hunting grounds;
- sacred sites; and
- other areas of economic, ceremonial and aesthetic value in accordance with their indigenous knowledge systems and practices and customary laws and traditions, and duly adopted Ancestral Domain Sustainable Development and Protection Plan ("ADSDPP") where ADSDPPs have been adopted, and to equitably benefit from the fruits thereof.

In all instances, ICCs/IPs shall have priority in the development, extraction, utilization and exploitation of natural resources.

4. Right to Benefits

The ICCs/IPs have the right to benefit from the utilization, extraction, use and development of lands and natural resources within their ancestral lands/domains and to be compensated for any social and/or environmental costs of such activities.

Accordingly, the concerned ICC/IP community shall be extended all the benefits already provided under existing laws, administrative orders, rules and regulations governing particular resource utilization, extraction or development projects/activities, without prejudice to additional benefits as may be negotiated between the parties.

II. INVESTMENT GUARANTEES AND INCENTIVES

Under the Mining Act, contractors under mineral agreements are given the following investment guarantees:

- Repatriation of Investments - The right to repatriate the entire proceeds of the liquidation of the foreign investment in the currency in which the investment was originally made and at the exchange rate prevailing at the time of repatriation.
- Remittance of Earnings - The right to remit earnings from the investment in the currency in which the foreign investment was originally made and at the exchange rate prevailing at the time of remittance.
- Foreign Loans and Contracts - The right to remit at the exchange rate prevailing at the time of remittance such sums as may be necessary to meet the payments of interest and principal on foreign loans and foreign obligations arising from financial or technical assistance contracts.
- Freedom from Expropriation - The right to be free from expropriation by the Government of the property represented by investments or loans, or of the property of the enterprise except for public use or in the interest of national welfare or defense and upon payment of just compensation. In such cases, foreign investors or enterprises shall have the right to remit sums received as compensation for the expropriated property in the currency in which the investment was originally made and at the exchange rate prevailing at the time of remittance.
- Requisition of Investment - The right to be free from requisition of the property represented by the investment or of the property of the enterprises except in case of war or national emergency and only for the duration thereof. Just compensation shall be determined and paid either at the time or immediately after cessation of the state of war or national emergency. Payments received as compensation for the requisitioned property may be remitted in the currency in which the investments were originally made and at the exchange rate prevailing at the time of remittance.
- Confidentiality - Any confidential information supplied by the contractor pursuant to the Mining Act and its Implementing Rules and Regulations shall be treated as such by the DENR and the Government during the term of the project.

The contractors in mineral agreements, and FTAAs shall be entitled to the applicable fiscal and non-fiscal incentives as provided for under the Omnibus Investments Code ("OIC"). In the same manner, holders of exploration permits may be entitled to the fiscal incentives granted under the OIC for the duration of the permits or extensions thereof.

To avail of the incentives, mining companies must register with the Board of Investments ("BOI"). The OIC through tax exemption and other benefits, encourages investments in preferred areas of economic activity specified by the BOI in the Investment Priorities Plan ("IPP"). In recognition of the value of the mining industry in the economic development of the country, the Philippine Mining Act mandates that mining activities shall always be included in the annual IPP.

The incentives under the OIC are generally available only to citizens of the Philippines or to domestic corporations owned and controlled by Philippine nationals. However, the nationality requirement is waived if the applicant will either export at least 70% of its total production or engage in a pioneer project. A pioneer enterprise either manufactures goods that have not been heretofore produced in the Philippines on a commercial scale, or employs a technology, formula, process or production scheme that has not been tried in the Philippines.

However, when the BOI waives the nationality requirement, the applicant should attain the status of a Philippine national (i.e., for corporations, at least 60% of the capital stock outstanding and entitled to vote must be owned and held by Philippine citizens) within 30 years from the date of its registration or such longer periods as may be determined by the BOI. However, a registered enterprise exporting 100% of its production need not comply with this divestment requirement.

An enterprise registered with the BOI enjoys the following tax and non-tax incentives:

A. Tax Incentives

1. Income tax holiday consisting of income tax exemption for six years from commercial operation for pioneer firms, and for four years for non-pioneer firms. This may be extended in the following instances:

- the project uses indigenous raw materials at rates set by the BOI; or
- the project meets the prescribed ratio of capital-equipment-to-number-of-workers set by the BOI; or
- the net foreign exchange savings or earnings amount to at least US$500,000 annually during the first three years of operation.

Expanding firms are entitled to an exemption from income taxes proportionate to their expansion for a period of three years from commercial operation. However, they are not entitled to additional deductions for incremental labor expenses during the period they avail of this incentive. A pioneer firm cannot avail of the income tax holiday for more than eight years.

2. Exemption from taxes and duties on imported spare parts and consumable supplies for export producers with Customs Bonded Manufacturing Warehouse exporting at least 70% of its production.

3. For the first five years from registration, an additional deduction from taxable income of 50% of the wages of additional skilled and unskilled workers in the direct labor force. This incentive is granted only if the

registered enterprise meets a prescribed capital to labor ratio and cannot be availed of simultaneously with the income tax holiday.

4. Exemption from taxes and duties on the importation of breeding stocks and genetic materials within 10 years from the date of registration or commercial operation.

5. Tax credit for taxes and duties on raw materials, supplies and semi-manufactured products used in the manufacture of export products and forming part thereof.

6. For registered enterprises with bonded manufacturing warehouses, exemption from taxes and duties on imported supplies and spare parts for consigned equipment.

7. Exemption from the wharfage duties and any export tax, duty, impost and fees within 10 years from date of registration.

8. Exemption from local taxes for six years from date of registration for pioneer enterprises and for four years from registration for non-pioneer enterprises

B. Non-tax Incentives

1. Simplified customs procedures for the importation of equipment, spare parts, raw materials and supplies and the export of processed products.

2. No restrictions for the use of consigned equipment. A re-export bond is required.

3. Employment of foreign nationals in supervisory, technical or advisory positions for five years from registration, extendible for limited periods. The president, general manager and treasurer (or their equivalent) of foreign registered firms are not subject to the foregoing limitations.

4. The privilege to operate bonded manufacturing/trading warehouses subject to customs rules and regulations.

III. TAX REGIME

The National Internal Revenue Code of the Philippines ("Tax Code") provides the general framework for the corporate tax regime observed in the Philippines. Under the Tax Code, corporations created or organized under Philippine laws are classified as *domestic corporations*. The term *domestic corporations* includes partnerships, no matter how created or organized, joint-stock companies, joint accounts, associations or insurance companies, but does not include general professional partnerships and a joint venture or consortium formed for the purpose of undertaking construction projects or engaging in petroleum, coal, geothermal and other energy operations pursuant to an operating or consortium agreement under a service contract with the Philippine government.

A. Income Tax

Domestic corporations are generally subject to Philippine income tax at the rate of 32% on their *taxable income* derived during the tax year from *all* sources within the Philippines and abroad. *Taxable income* refers to the pertinent items of gross income specified in the Tax Code, less the deductions authorized by the Tax Code for such types of income. Gross income includes income derived from the conduct of trade or business, gains derived from dealings in property, interests, rents, royalties,

dividends, among others. On the other hand, allowable deductions include ordinary and necessary business expenses, interest, taxes, losses, bad debts, depreciation, charitable and other contributions.

The Tax Code also imposes a Minimum Corporate Income Tax ("MCIT") of 2% of the gross income as of the end of the taxable year, on domestic and resident foreign corporations subject to normal income tax rates. A corporation is liable to pay the MCIT only when:

- the corporation has zero or negative taxable income; or
- the amount of MCIT is greater than the normal income tax due from such corporation.

The Tax Code allows any excess of the MCIT over the normal income tax to be carried forward on an annual basis and credited against the normal income tax for three immediately succeeding taxable years.

For purposes of computing the tax base for the MCIT, the Tax Code defines *gross income* as gross receipts less sales returns, discounts and allowances, and cost of goods or services sold, as the case may be. *Cost of goods* sold includes all business expenses directly incurred to produce the merchandise and to bring such merchandise to their present location or use.

The MCIT will be imposed beginning the 4th taxable year immediately following the taxable year in which the corporation commenced its business operations. For purposes of the MCIT, the taxable year in which business operations commenced shall be the year in which the corporation registered with the BIR.

1. Allowable Deductions for Mining Companies

Aside from business expenses and similar deductions from gross income, the Tax Code allows mining contractors to claim as a tax deduction an allowance for depreciation in respect of all properties used in mining operations, computed as follows:

- at the normal rate of depreciation if the expected life is 10 years or less; or
- depreciated over any number of years between five years and the expected life if the latter is more than 10 years, and the depreciation thereon allowed as deduction from taxable income; *provided*, that the contractor notifies the Bureau of Internal Revenue ("BIR") at the beginning of the depreciation period which depreciation rate will be used.

The Tax Code also permits mining companies to claim as a tax deduction a reasonable allowance for depletion or amortization computed in accordance with the cost-depletion method in accordance with rules and regulations prescribed by the Department of Finance, upon recommendation of the Commissioner of the BIR, and which should not exceed the capital invested. After production in commercial quantities has commenced, certain intangible exploration and development drilling costs shall be:

- deductible in the year incurred if such expenditures are incurred for non-producing wells and/or mines; or
- deductible in full in the year paid or incurred or, at the election of the taxpayer, may be capitalized or amortized if such expenditures incurred are for producing wells and/or mines in the same contract area.

Any intangible exploration, drilling and development expenses allowed as a deduction in computing taxable income during the year shall not be taken into consideration in computing the adjusted cost basis for the purpose of computing allowable cost depletion.

In computing taxable income from mining operations, the Tax Code gives the taxpayer the option to deduct exploration and development expenditures accumulated as cost or adjusted basis for cost depletion as of the date of prospecting, as well as exploration and development expenditures paid or incurred during the taxable year. However, the total amount deductible for exploration and development expenditures cannot exceed 25% of the net income from mining operations computed without the benefit of any tax incentives. The actual exploration and development expenditures minus 25% of the net income from mining can be carried forward to the succeeding years until fully deducted. The election of the taxpayer to deduct the exploration and development expenditures is irrevocable and binding in succeeding taxable years.

For purposes of the foregoing, the term "net income from mining operations" refers to gross income from operations less allowable deductions that are necessary or related to mining operations such as mining, milling and marketing expenses, and depreciation of properties used directly in mining operations. The term "exploration expenditures" means expenditures paid or incurred for the purpose of ascertaining the existence, location, extent, or quality of any deposit of ore or other mineral, and paid or incurred before the beginning of the development stage of the mine or deposit. On the other hand, the term "development expenditures" refers to expenditures paid or incurred during the development stage of the mine or other natural deposits.

B. Tax on Dividends

Distributions made by a domestic corporation out of its earnings or profits, whether in money or other property, which are payable to its shareholders are classified as *dividends*. Dividends received by a domestic corporation or a resident foreign corporation (i.e., a foreign corporation engaged in trade or business in the Philippines) from another domestic corporation are not subject to Philippine income tax. On the other hand, dividends received by a non-resident foreign corporation not engaged in trade or business in the Philippines are generally subject to Philippine income tax at the rate of 32% of the gross amount of the dividends. The 32% tax on dividends is a final withholding tax, i.e., the Philippine corporation has the obligation to withhold the amount of the tax from the gross amount of the dividends and to remit such tax to the BIR on behalf of the non-resident foreign corporation.

Under the Tax Code, the income withholding tax rate on dividends may be reduced to 15% if either of the following conditions is present:

- The country in which the non-resident foreign corporation is domiciled allows a credit against the tax due from the non-resident foreign corporation's taxes deemed to have been paid in the Philippines, equivalent to at least 17%; or
- The country in which the non-resident foreign corporation is domiciled does not impose any income tax on dividends received from the Philippine corporation.

The income withholding tax rate on dividends may also be reduced under Philippine tax treaties with countries where the non-resident foreign corporation is

domiciled. To confirm the application of the reduced withholding tax rate on Philippine dividends, an application for relief from double taxation must be filed with the BIR.

C. Excise Tax

The Tax Code also imposes an excise tax on minerals, mineral products and quarry resources, as follows:

- On coal and coke, a tax of Php10 per metric ton;
- On all non-metallic minerals and quarry resources, a tax of 2% based on the actual market value of the gross output thereof at the time of removal, in the case of those locally extracted or produced; or the value used by the Bureau of Customs in determining tariff and customs duties, net of excise tax and value-added tax, in the case of importation;
- On all metallic minerals, a tax of 2% based on the actual market value of the gross output thereof at the time of removal, in the case of those locally extracted or produced; or the value used by the Bureau of Customs in determining tariff and customs duties, net of excise tax and value-added tax, in the case of importation;
- On indigenous petroleum, a tax of 3% of the fair international market price thereof, on the first taxable sale, barter, exchange or such similar transaction, such tax to be paid by the buyer or purchaser before removal from the place of production.

D. Value-Added Tax

The Tax Code also imposes value added tax ("VAT") on any person (whether individual or corporate) who, in the course of trade or business, sells, barters, exchanges, leases goods or properties and renders services, and any person who imports goods into the Philippines.

The VAT is generally imposed on the sale of goods, properties and services at the standard rate of 10%. For sales of goods subject to VAT, the 10% rate is imposed on the "gross selling price" or the total amount of money or its equivalent, which the purchaser pays or is obligated to pay to the seller in consideration of the sale, barter or exchange of the goods or properties.

The Tax Code also imposes 10% VAT on *every* importation of goods based on the total value used by the Philippine Bureau of Customs in determining tariff and customs duties, plus customs duties, excise taxes, if any, and other charges. The importer has the obligation to pay VAT on its importation. The 10% VAT must be paid, along with the other import duties and charges, before the imported goods may be released from customs custody.

VAT is in the nature of an indirect tax, i.e., the amount of the VAT payable by the seller may be shifted or passed on to the buyer or importer of goods as an increment to the price of the goods. The buyer may then apply the VAT passed on to it by the seller as an input tax credit. In other words, the buyer or lessee may deduct the VAT passed on to it against its own VAT liabilities, if any.

For every sale of goods or services, VAT-registered persons are also required to issue receipts or sales/commercial invoices duly registered with the BIR. The issuance of duly registered receipts and invoices is necessary for a VAT taxpayer to validly claim tax credits to lessen its VAT liabilities.

In certain transactions by VAT-registered persons, VAT at the rate of 0% is imposed as a form of tax incentive. The so-called "zero-rated sales" generally refer to export sales of raw materials, foreign currency denominated sales, sale of gold to the *Bangko Sentral ng Pilipinas*, and sales to entities enjoying exemptions under special laws and international agreements. Tax credits arising from purchases connected with such zero-rated sales may be claimed as refunds from the BIR if the tax credits are unutilized by the seller.

The Tax Code also enumerates transactions, which are exempt from VAT. These VAT-exempt transactions include the sale or importation of coal and natural gas, in whatever form or state, and petroleum products (except lubricating oil, processed gas, grease, wax and petrolatum) subject to excise tax. Unlike taxpayers whose sales are subject to 0% VAT, sellers of goods, properties and services who engage in VAT-exempt sales cannot claim tax credits on purchases connected with such sales.

IV. ENVIRONMENTAL LAWS

The Philippines adheres to a policy of protecting and advancing the right of its people to a balanced and healthful ecology. The DENR is the lead agency in environmental protection and administration. The DENR's Environmental Management Bureau ("EMB"), local government units and other agencies also assist in the formulation and implementation of environmental policies.

The relevant environmental laws and regulations are as follows:

A. Environmental Impact Statement ("EIS") System

The EMB is the lead agency that implements the EIS System and handles the review and evaluation of the environmental impact of development projects. Under the EIS System, a project proponent of environmentally critical projects and projects within environmentally critical areas must obtain an environmental compliance certificate ("ECC") prior to the commencement of the project. Under DENR regulations, resource-extractive industries, including mining, are considered environmentally critical projects.

An ECC certifies that a proposed project or undertaking will not cause significant negative environmental impact. The ECC also certifies that the proponent has complied with all the requirements of the EIS System and has committed to implement its approved Environmental Management Plan. The ECC contains specific measures and conditions that the project proponent has to undertake before and during the operation of a project, and in some cases, during the project's abandonment phase to mitigate identified environmental impacts.

B. Ecological Solid Waste Management Act

The Ecological Solid Waste Management Act ("Solid Waste Act") provides for a national program that will manage the control, transfer, transport, processing and disposal of solid waste in the country. Certain acts are prohibited under the Solid Waste Act, as follows:

- Dumping waste matters in public places such as roads, canals or sidewalks;
- Open burning of solid waste;
- Permitting the collection of non-segregated waste;
- Squatting in open dumps and landfills;

- Open dumping in flood-prone areas;
- Mixing of source-separated recyclable material with other solid waste in any container for solid waste collection;
- Operating of open dumps, outside the provisions of the law;
- Manufacturing or distributing non-environmentally acceptable packaging materials;
- Importing consumer products in non-environmentally acceptable packaging materials;
- Importing toxic wastes misrepresented as recyclable;
- Transporting and dumping in bulk of collected domestic, commercial, industrial and institutional wastes outside of designated centers or facilities;
- Preparing, expanding, constructing or operating waste management facilities without an Environmental Compliance Certificate and without conforming to the land use plan of the LGU;
- Constructing any establishment within 200 meters from open or controlled dumpsites or sanitary landfills; and
- Constructing or operating any landfills or waste disposal facility on any area or portion of an aquifer, water reservoir or watershed.

Violation of the provisions of the Solid Waste Act is punishable by a fine and/or imprisonment.

C. Toxic Substances and Hazardous and Nuclear Wastes Control Act

The Toxic Substances and Hazardous and Nuclear Wastes Control Act ("The Hazardous Waste Act") provides the legal framework for the country's program to control and manage the importation, manufacture, processing, distribution, use, transport, treatment, and disposal of toxic substances and hazardous and nuclear wastes.

The Hazardous Waste Act requires all manufacturers and importers of a new chemical to submit a pre-manufacture and pre-importation notification ("PMPIN") to the DENR. A "new chemical substance" is defined as any chemical that is not included in the Philippine Inventory of Chemicals and Chemical Substances ("PICCS"). The purpose of the PMPIN is to screen harmful substances before they enter the Philippines. The PICCS is a list of existing industrial chemicals and chemical substances used, sold, distributed, imported, processed, manufactured, stored, exported, treated, or transported in the Philippines.

Manufacturers and importers of new chemicals are required to notify the DENR of their intent to manufacture or import the new chemical within 90-180 days before commencing the manufacture or importation of the new chemical. Together with this notification, the proponent must submit the appropriate PMPIN forms.

Once a chemical is listed in PICCS, it may be manufactured or imported with no control, provided it is not included in the Priority Chemicals List ("PCL") or subject to a Chemical Control Order ("CCO").

The PCL is a short list of chemicals that have been determined to potentially pose unreasonable risks to public health, workplace, and environment. Inclusion in the

PCL is based on the selection criteria used by industrialized countries, such as persistence, toxicity, and bioaccumulation. Users, importers and manufactures of chemicals listed in the PCL are required to comply with various registration and reporting requirements.

A CCO prohibits, limits or regulates the use, manufacture, import, export, transport, processing, storage, possession and wholesale of priority chemicals that are determined to be regulated, phased-out, or banned because of the serious risks they pose to public health, the work place and the environment. The objective of a CCO is to ensure the proper management of the chemicals so that danger to human health and the environment is reduced. A CCO specifies requirements for the importation, manufacturing, use, transport and disposal of these chemicals. A CCO also requires the subsequent phase-out of the chemical and its substitution with less harmful chemicals.

Violation of the provisions of the Hazardous Waste Act is punishable by a fine and/or imprisonment as well as administrative fines.

D. Clean Air Act

The Clean Air Act provides for a comprehensive management program for air pollution. Under the implementing rules and regulations of the Clean Air Act, all stationary sources of air pollution must have a valid permit to operate issued by a DENR Regional Director. New or modified sources must obtain an authority to construct from the Director. However, the DENR may reduce penalties or fines to be imposed on stationary sources provided the latter execute a consent agreement with the EMB and implement an environmental management plan with a timetable specified

The following acts are prohibited under the Clean Air Act and its implementing rules and regulations:

- Causing or allowing the emission of particulate matter from any source whatsoever without taking reasonable precautions to prevent such emissions.
- Storing, pumping, handling, processing, unloading or using in any process, or installing volatile compound or organic solvents without applying known existing vapor emission control devices or systems deemed necessary and approved by the EMB.
- Discharging from any source whatsoever such quantities of air contaminants or other material that constitute nuisance as defined under the law.
- Burning any materials in any quantities which will cause the emission of toxic and poisonous fumes.
- Open burning of waste.
- Incineration, which is the burning of municipal, bio-medical and hazardous wastes, emitting toxic and poisonous flames, is prohibited

Industries which will install pollution control devices or retrofit their existing facilities with mechanisms that reduce pollution, will be entitled to tax incentives such as but not limited to tax credits and/or accelerated depreciation deductions.

The violation of the Clean Air Act has a corresponding penalty of fine or imprisonment.

E. Clear Water Act

The Clean Water Act applies to water quality management in all water bodies. However, it applies primarily to the abatement and control of pollution from land-based sources. This notwithstanding, the water quality standards and regulations and the civil liability and penal provisions under the Clean Water Act will be enforced irrespective of sources of pollution.

The following acts, among others, are prohibited under the Clean Water Act:

- Discharging, depositing or causing to be deposited material of any kind directly or indirectly into the water bodies or along the margins of any surface water, where, the same will be liable to be washed into such surface water, either by tide action or by storm, floods or otherwise, which could cause water pollution or impede natural flow in the water body;
- Discharging, injecting or allowing to seep into the soil or sub-soil any substance in any form that would pollute groundwater. In the case of geothermal projects, and subject to the approval of the DENR, regulated discharge for short-term activities (e.g., well testing, flushing, commissioning, venting, etc.) and deep re-injection of geothermal liquids may be allowed. However, safety measures should be adopted to prevent the contamination of the groundwater;
- Operating facilities that discharge regulated water pollutants without the valid required permits or after the permit was revoked for any violation of any condition therein;
- Unauthorized transport or dumping into sea waters of sewage sludge or solid waste as defined under the Solid Waste Act;
- Transport, dumping or discharge of prohibited chemicals, substances or pollutants listed under the Hazardous Waste Act;
- Operate facilities that discharge or allow to seep, willfully or through gross negligence, prohibited chemicals, substances or pollutants listed under the Hazardous Waste Act, into water bodies or wherein the same shall be liable to be washed into such surface, ground, coastal, and marine water;
- Undertaking activities or development and expansion of projects, or operating wastewater/sewerage facilities in violation of Presidential Decree No. 1586 and its implementing rules and regulations;
- Discharging regulated water pollutants without the valid required discharge permit pursuant to the Clean Water Act or after the permit was revoked for any violation of any condition therein.

A violation of the Clean Water Act may be penalized by fine and/or imprisonment.

F. Pollution Control Law

Under the Pollution Control Law, it is unlawful for a person to dispose any organic or inorganic matter or any substance in gaseous or liquid form that may cause water pollution in any Philippine water resource.

G. Water Code

The Water Code prohibits any person from building any works that may produce dangerous or noxious substances, or performing any act, which may result in the

introduction of sewage, industrial waste, or any pollutant into any source of water supply without prior permission from the EMB.

H. National Environmental User's Fee of 2002 ("NEUF")

The NEUF applies to all establishments and installations that discharge industrial and commercial wastewater into water bodies and/or land resources.

Any person who will discharge in any manner industrial or commercial wastewater into Philippine water and/or land resources must secure a wastewater discharge permit from the relevant Regional Office of the EMB. A wastewater discharge permit fee will also be assessed (fixed fee and load-based fee).

Quisumbing Torres
12th Floor, Net One Center
26th Street corner 3rd Avenue
Crescent Park West, Bonifacio Global City
Taguig, Metro Manila
Philippines 1634
Phone: (63) 2 819 4700
Fax: (63) 2 816 0080; 728 7777
QTLaw@bakernet.com

Quisumbing Torres is a member firm of Baker & McKenzie International, a Swiss Verein with member law firms around the world. In accordance with the common terminology used in professional service organizations, reference to a “partner” means a person who is a partner, or equivalent, in such a law firm. Similarly, reference to an “office” means an office of any such law firm.

©2005 Quisumbing Torres
All rights reserved.