Chandrawat & Partners

Doing business in Philippines

A comprehensive guide on doing business

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OVERVIEW

The Philippines is an emerging market and a newly industrialized country, whose economy is transitioning from being agricultural to service- and manufacturing-centered. It is a founding member of the United Nations, the World Trade Organization, ASEAN, the Asia-Pacific Economic Cooperation forum, and the East Asia Summit. It is a popular destination for business process outsourcing (BPO).

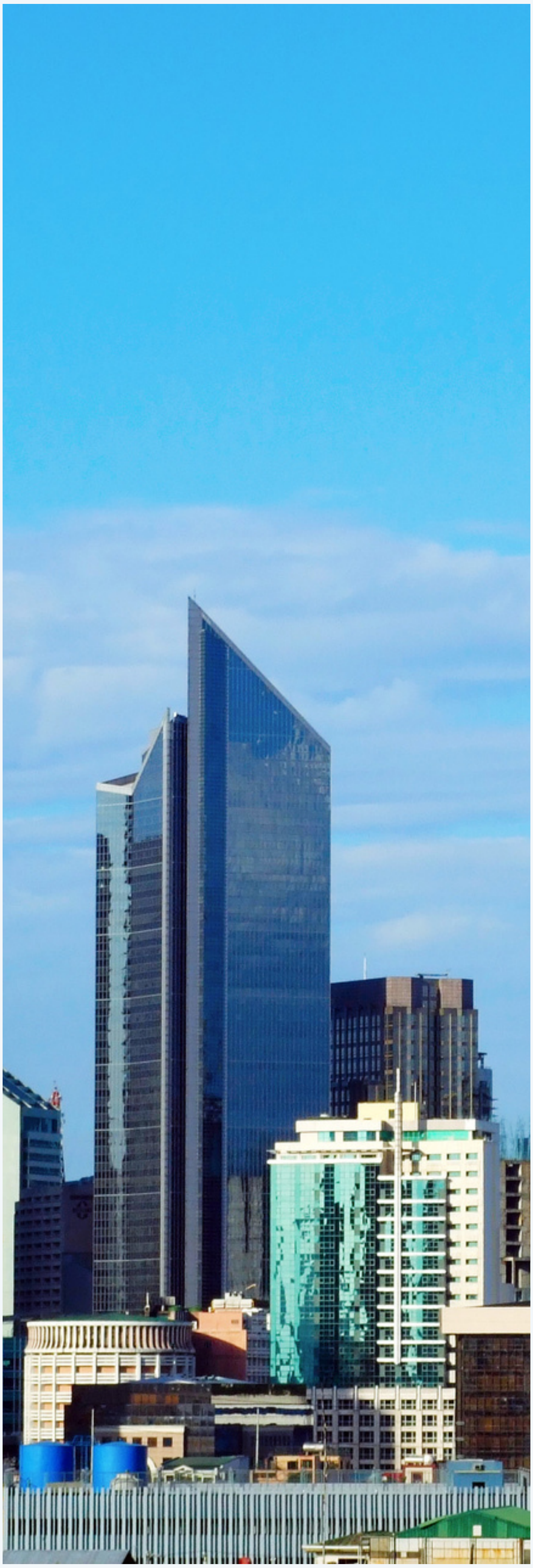
The Philippines is an ideal country for companies looking to expand internationally. Their economy has consistently been among the fastest growing in the ASEAN region, making it one of the quickest growing markets globally. With a highly proficient English-speaking population that is eager to work abroad and collaborate with foreign businesses, the Philippines' workforce thrives in global services and trade.

Philippine economy potentially faces an even faster, sustained and more inclusive growth, as the country enters its "demographic sweet spot" which is expected to last until 2050. The discussion has been around Philippine legal system, foreign investment, including restrictions, currency regulations and incentives. Laws in regulations of employment relationships, swift overviews on competition law and safety are also included.

Also summarized are taxations and tax residencies, Overall, the nation boasts an educated workforce, a strategic business location, a steadily expanding infrastructure and a highly developed, business-friendly economy with practically unlimited opportunities for companies looking to expand there.

ECONOMIC OVERVIEW

The economy of the Philippines is an emerging market, a newly industrialized country and one of the most dynamic in Asia-Pacific region. As a developing economy, the country is working towards achieving greater industrialization and economic growth. The Philippine economy is the world's 36th largest by nominal Gross Domestic Product ("GDP") and 15th largest in Asia according to the international monetary fund in 2023. The Philippine economy is transitioning from one based on agriculture to one based more on services and manufacturing. It has experienced significant economic growth and transformation in recent years.



The Philippines posted a high GDP growth rate of 7.6 percent in 2022. However, the country is not a part of the Group of 20 nations; instead, it is grouped in a second tier for emerging markets or newly industrialized countries. As a newly industrialized country, the Philippines is still an economy with a large agricultural sector; however, the country's service industry has expanded recently. Much of the industrial sector is based on processing and assembly operations in the manufacturing of electronics and other high-tech components, usually from foreign multinational corporations.

Over the decade ahead, rapid economic growth is forecast for the Philippines economy. By 2034 the Philippines is set to join the ranks of a small group of countries in the Asia-Pacific region that have a GDP exceeding one trillion dollars. This will result in a significant transformation of the structure of the Philippines economy, with substantial expansion in the size of the domestic consumer market. This will also help to drive foreign direct investment inflows into the Philippines, as multinationals build up their local presence.

FOREIGN DIRECT INVESTMENT

According to the UNCTAD's World investment report 2022, foreign direct investment inflows to the Philippines increased from USD 6.8 billion in 2020 to USD 10.5 billion in 2021, remaining above the full-year target of USD 8 billion set by the Central Bank of the Philippines. The stock of FDI also increased in 2021, reaching USD 113 billion. The United States, China, the United Kingdom, Singapore, and Japan are traditionally the main investors, while inflows are concentrated in the transportation and storage, electricity, real estate, manufacturing, and construction.

Other sectors that attract the highest levels of investment are information and communication, and administrative and business support services activities. Moreover, the country relaxed the local employment requirement for workers of foreign investors. Furthermore, the Philippines have been substantially improving its business climate in recent years: starting a business is now easier due to the abolishment of the minimum capital requirement for domestic companies; dealing with construction permits has been improved (improvement of coordination, standardization of the process for obtaining an occupancy certificate); and minority investor protection has also been strengthened.

Foreign investors who wish to benefit from investment incentives may register with either the Philippine Economic Zone Authority ("PEZA") or the Board of Investments ("BOI"). The PEZA grants incentives to businesses engaged in exports that are located within identified economic zones. The board of investment, on the other hand, administers the grant of incentives to businesses engaging any of the investment priority areas provided under the investment priorities plan. The administration aims to create a self-sufficient Philippines. Thus, longer benefits are granted to industries such as agriculture to promote food security, healthcare to better withstand future pandemics, power to reduce reliance on imported fuel, and higher tier activities.

Some of the incentives granted are exemptions from the payment of tariff and customs duties and other taxes and fees, income tax holiday and reduced tax rates. Telecommunications and other vital services are subject to safeguards for critical structure and the reciprocity rule. On the other hand, the amended Retail liberalization Act grants foreign enterprises the right to invest in retail trade businesses with a minimum paid-up capital of P25 million. If it owns more than one physical store, the investment per store should be at least P10 million.

ADVANTAGES

Strategic location

Set at the junction of eastern and western businesses, the Philippines is at the heart of Asia's fastest-growing region and is thus a critical point of entry into the ASEAN market and a gateway to international shipping for European and American companies. In addition, several notable financial centers are located nearby, including Singapore, Tokyo, Hong Kong, Taipei, and Bangkok. The U.S. government's strategic focus on the region and its decades-long ties with the Philippines present significant opportunities to support an Indo-Pacific partnership based on democratic values and free trade while advancing the Philippines' quest for self-sufficiency.

Trade considerations

The Philippines and several other countries across the world have signed free trade agreements that cover trade in goods and services, government procurement, investment, competition, intellectual property, business, and sustainable development. A free trade agreement is designed to boost trade between two or more nations allowing goods and services to cross borders without government tariffs, quotas, subsidies, or prohibitions. This is particularly important for businesses looking to expand to the Philippines.

Unlimited business opportunities

The ASEAN Free Trade Agreement ("AFTA") has integrated Asia's economies into one giant market, making the Philippines an ideal location for businesses that want access to this market. It has enhanced and primed various areas for investors while also allowing customers to choose from a wide range of products. Over the years, trade and investment events have influenced the country's industrialization process. Additionally, the Philippines has signed treaties, trade agreements, and memorandum of understanding with more than 35 countries across the globe. Today, the Philippines has adopted a multitrack liberalization approach, making it one of AFTA's top choice countries.

Access to talent

Among the Philippines' most compelling advantages to foreign businesses looking to expand there is its large pool of highly educated local talent. As one of one of the world's largest English-speaking countries, the nation has a literacy rate of 97.5%, with over half a million university graduates entering the workforce each year. This coupled with an extremely business-friendly environment makes workers in the Philippines extremely adaptable. This is part of the reason why the Philippines has traditionally been the location of choice for U.S., Australian, and British companies seeking to employ offshore talent.

KEY SECTORS

Business process outsourcing

The economic contribution of the Philippines' BPO industry is expected to outpace further remittances sent from Filipinos working abroad. Remittances were an important stabilizing factor for the country's economy during the height of the pandemic in 2020 and 2021, contributing to some 10 percent of GDP, making the Philippines the country with the highest remittances to GDP ratio in Southeast Asia. Remittances to the Philippines hit a record high of US$36 billion in 2022. However, it is expected that the ratio of remittances will begin to decrease as revenue from local industries such as BPO begins to fill the gap. For instance, revenue from BPO activities now contributes to approximately 11 percent of GDP.

Electronics and semiconductors

Philippines' electronics sector is one of the biggest contributors and the backbone of the country's manufacturing output. The export of electronics and semiconductors are expected to reach US$50 billion in exports for 2023, rising from US$45.92 billion in 2022. The electronics industry is classified into 73 percent semiconductor manufacturing services and 27 percent electronics manufacturing. Through greater foreign investments, the Philippines is also aiming to attract investments that will move up the global value chain.

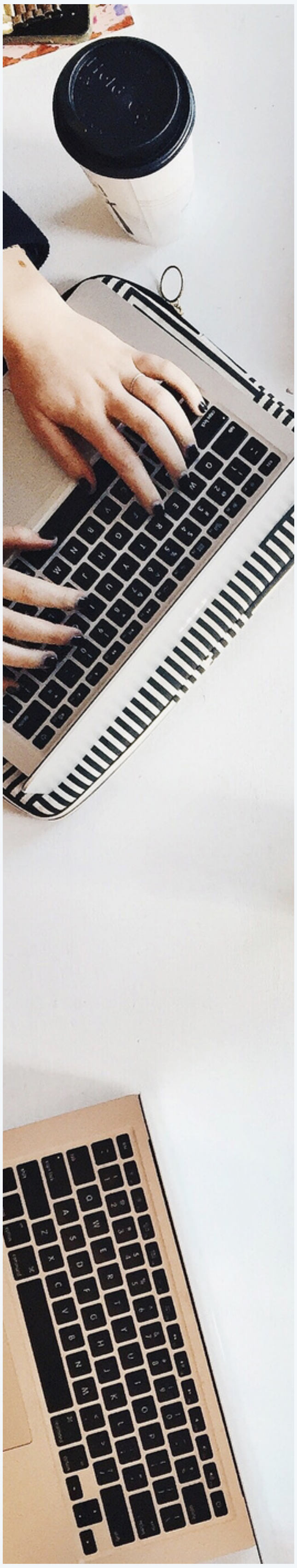
Agriculture

The value of the top 10 agricultural exports in the Philippines was valued at US$6.49 billion in 2022. The country's main agricultural products include rice, coconuts, sugarcane, corn, bananas, pineapples, and mangos. The sector also contributes to an estimated 8.9 percent of GDP in 2022 and employs 24 percent of the local workforce. However, agriculture has only grown around two percent per year in real terms, compared with the economy's five percent growth. The country is encouraging investments in areas like AgriTech to not only drive-up yields but also improve irrigation and infrastructure to reduce export-related costs and food wastage. A three-year agriculture development program is currently in the works with the aim to promote agricultural productivity, particularly in rice, corn, high-value crops, poultry, fisheries, and livestock.

The digital economy

There are significant opportunities for foreign investors in the Philippines' e-commerce sector, which has been the main growth driver of the country's digital economy. Foreign investors can also provide solutions in cloud computing, financial technology (FinTech), the internet of things, and big data for various Filipino industries. Importantly, FinTech can help improve financial inclusivity in the country, serving the underbanked and unbanked population. Moreover, many micro, small, and medium-sized businesses have little access to formal financing from banks because many are operating in the informal sector, and as a result, they do not pass the stringent requirements from banks.

TYPES OF BUSINESS



Sole proprietorship

A sole proprietorship is the most basic type of business structure in the Philippines because it's the simplest to set up. Sole proprietors such as general merchandise stores, small retail establishments, and ready-to-wear shops are liable for the business's liabilities, debt, and losses. Little paperwork is needed as owners only need to apply for a business name and register their business with the Department of Trade and Industry ("DTI").

Partnership

A partnership business structure is formed by two or more people who agree to do business together to gain profit. Partnerships are most commonly seen in law firms, real estate investment networks, and physician groups. The owners contribute to the company through skill, funding, labor, or something similar, and they also share the revenue.

Limited partnership

Limited partners are only responsible for the sum invested in the partnership. Compared to general partners, limited partners have no management rights or input into company operations.

Corporation

A corporation in the Philippines is treated legally as a personality separate, distinct from the stockholders who own the corporation. A total of 15 people is needed to open a lawful corporation. This structure requires close coordination with the Securities and Exchange Commission ("SEC") and involves multiple record-keeping and accounting work.

There are two kinds of a corporation:

- Stock corporation
- Non-stock corporation

One-person corporation

A one-person corporation ("OPC") only has one stockholder who can be a natural person, trust, or estate. It combines the best aspects of a corporation and a sole proprietorship, namely limited liability and complete dominion. These typically include banks, pre-need trust and insurance companies.

COMPANY REGISTRATION

In order to register a company in the Philippines, an entrepreneur must pay the necessary fees associated with incorporating the business. Here are the various fees that must be paid by an entrepreneur for company registration in the Philippines:

- SEC enrollment charges: Total Securities and Exchange Commission ("SEC") charges for Philippines company registration is PHP 6,750.
- Bureau of internal revenue cost: The overall cost for bureau of internal revenue registration is PHP 530.
- Department of trade and industry: The overall fee for enrollment with the department of trade and industry is PHP 1700.

1

Register the business name

The first step for Philippines company registration is to decide on a name for your business and register it with the SEC. A business name can be registered and reserved online with the SEC by setting up an account.

2

Gather the documents

The entrepreneur must next compile and collect the necessary paperwork before submitting it to the securities and exchange commission in order to register a company in the Philippines. The documents to be submitted include the articles of incorporation, the bylaws of the firm, and the treasurer's affidavit.

3

Acquire the business licenses and permits

The entrepreneur must also secure various licenses before starting any commercial operations. The business owner must request the barangay's clearance, mayor's permit, and a business license.

4

Enroll with the Bureau of Internal Revenue ("BIR")

One must enroll your new business with the Bureau of Internal Revenue (BIR) in order to comply with your tax requirements in the Philippines and obtain the tax identification number.

5

Enroll with the government agencies

If the company wishes to recruit workers, it must enroll as an employer with the following governmental bodies:

- Social security system,
- PhilHealth
- Pag-IBIG Fund

HOW TO ESTABLISH AN ENTITY

There are 5 legal structures available for foreign businesses wishing to operate in the Philippines: (a) subsidiary, which is registered under the Philippine law and treated as a Philippine domestic corporation, (b) branch office, (c) representative office, (d) Regional or Area Headquarters ("RHQ") and (e) Regional Operating Headquarters ("ROHQ").

Incorporation Process

In general, Philippine corporations are required to file the following annual reports with the Securities and Exchange Commission ("SEC"):

- General Information Sheet ("GIS") must be filed within 30 calendar days of the annual stockholders' meeting,
- the Audited Financial Statements ("AFS"), as stamped received by the BIR, must be filed with the SEC within 120 calendar days from the end of the fiscal year according to the Financial Statements.

Branch offices and representative offices of foreign corporations, as well as ROHQs and RHQs, are likewise required to file the following with the SEC:

- a GIS within 30 days of the anniversary of the issuance of the SEC License; and
- the AFS, as stamped received by the BIR, within 120 calendar days from the end of the fiscal year according to the Financial Statements.

For domestic corporations, an amended GIS is submitted to the SEC for any relevant changes, including changes in the directors or officers of the corporation during the year. A notification update form is required for any change in the principal office address, officers or additional subsidiaries of branch offices and representative offices of foreign corporations, as well as ROHQs and RHQs.

The corporation's GIS shall include a beneficial declaration page in compliance with said SEC directive. Listed and public companies, as well as companies with secondary licenses, are subject to more stringent reportorial and disclosure requirements with the SEC, including required reports on changes in beneficial ownership of securities, and the submission of quarterly reports.

The incorporation of a local subsidiary requires at least 5 but not more than 15 incorporators; the majority of whom must be residents of the Philippines. Each of the incorporators must own or be a subscriber to at least 1 share of the capital stock of the company. At least 25% of the authorized capital stock, as stated in the articles of incorporation, must be subscribed at the time of incorporation, with at least 25% of the total subscription paid upon subscription.

TAXATION

The main taxes imposed on corporations in the Philippines are corporate income tax, value-added tax (“VAT”) and withholding tax (“WT”). Other taxes include percentage tax (generally for activities not subject to VAT), excise tax, documentary stamp tax, local business and real property taxes.

Corporate income tax of 30% is imposed on taxable income. In the 4th year of operations, the tax imposed is either 2% of gross income or 30% of taxable income, whichever is higher. For entities covered by special laws (for example, PEZA entities), a 5% income tax is imposed on the gross income. Regional Operating Headquarters on the other hand, are entitled to an income tax rate of 10% on taxable income. Quarterly income tax returns should be filed and the payment should be made, on or before the 60th day following the close of each of the quarters of the taxable year. The annual income tax return shall be filed and the payment made on or before the 15th day of April of each year covering taxable income for the preceding taxable year.

VAT at the rate of 12% is imposed on the sale, barter, exchange or lease of goods or properties and services in the Philippines, including the importation of goods. Being an indirect tax, the VAT can be passed on to the buyer or end user of the goods and/ or services. The VAT returns must be filed and the corresponding payment (if any) made within 20 days following the end of each month (for monthly VAT returns) and 25 days following the close of the taxable quarter (for quarterly VAT returns) unless the filer is enrolled under the Electronic Filing and Payment System (“EFPS”).

Tax rates range from 1% to 30%, depending on the nature of the payment. However, income payments to foreign entities may be subject to lower preferential tax treaty rates provided that a certificate of residence for tax treaty relief form has been accomplished before the payment of income is made. This form applies only to income payments for dividends, interests and royalties. Local business taxes, fees and charges are also levied by local government units (“LGUs”).

EMPLOYMENT POLICIES

Minimum wage: Under the Philippines' minimum wage law, the minimum wage rate varies from one region of the country to another and is set by the relevant regional tripartite wages and productivity board. Under the most recent wage order for the national capital region (i.e., Metro Manila), the minimum gross basic wage is PHP466 per day plus cost-of-living allowance of PHP15 per day.

Work hours and overtime: The normal hours of work should not exceed eight hours a day. Unless there is a valid compressed work week arrangement, an employee who renders work in excess of eight hours a day is entitled to overtime pay equivalent to the applicable wage rate plus at least 25 percent thereof. The overtime rate will vary if the overtime work is rendered on a rest day, regular holiday or special day or during the period between 10 p.m. and 6 a.m. of the following day.

Rest Days: An employer may require its employees to work six days per week. Employees, except exempt employees, are entitled to a rest period without pay of not less than 24 consecutive hours for every six consecutive normal working days. For work done on rest days, the employer should pay compensation equivalent to the applicable wage rate plus at least 30 percent thereof.

Service incentive leave: Except for exempt employees, every employee who has rendered at least one year of service is entitled to a yearly service incentive leave (which is commonly replaced by vacation leave) of five days with pay. The service incentive leave should be converted to its money equivalent and paid to the nonexempt employee by the employer if not used or exhausted by the said employee at the end of the year.

Maternity leave: Every qualified pregnant woman in the private sector is entitled to maternity leave of 60 days in case of normal delivery, abortion or miscarriage, or 78 days in case of caesarean delivery. During such leave, the pregnant woman shall receive daily maternity benefit equivalent to 100 percent of her average salary credit, computed based on the formula of the Social Security System ("SSS"), for 60 or 78 days, as the case may be.

13th month pay: All "rank-and-file" employees of employers covered by the revised guidelines on the implementation of the 13th Month Pay Law are entitled to a bonus called "13th month pay," regardless of the amount of their monthly basic salary, their designation or employment status, and the method by which their salary is paid, provided they have worked for at least one month during a calendar year.

HOW WE CAN HELP?

Our wealth of practical expertise guides companies throughout the entire business process. We deliver a range of services that help clients plan and complete the setting up of the business. These include:

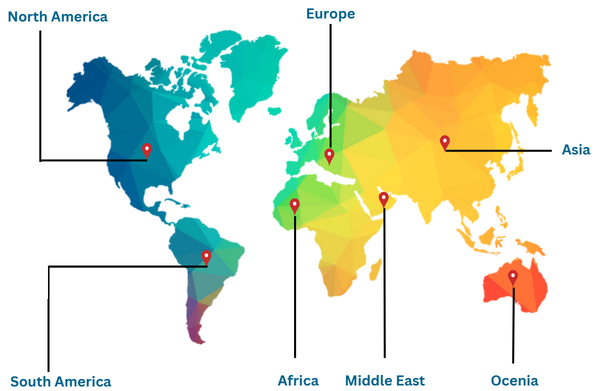
- Understand the local business culture: It is essential to take the time to understand local customs, etiquette, and business practices.

- Establish a local presence: Having a local presence can help establish credibility and build trust with customers and partners. This can include setting up a local office or partnering with a local company.
- Due diligence: Philippines has a complex legal and regulatory framework, and it is essential to comply with all applicable laws and regulations to avoid legal and regulatory risks

- Seek professional advice: We help our clients to seek professional advice from legal and business experts who have experience and knowledge of Philippines' laws, regulations, and business practices.

- Hire a local workforce: Hiring a local workforce can help navigate local regulations and cultural nuances. It is essential to comply with local labour laws and regulations when employing workers in Philippines.
- Shareholder services: We provide services for the purpose of holding in trusts, assets, usually shares, stocks, and bonds as nominees and custodians. We assist in registering trusts for the shares in our client’s business in the name of our nominee shareholder.

SERVING CLIENTS WORLDWIDE



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