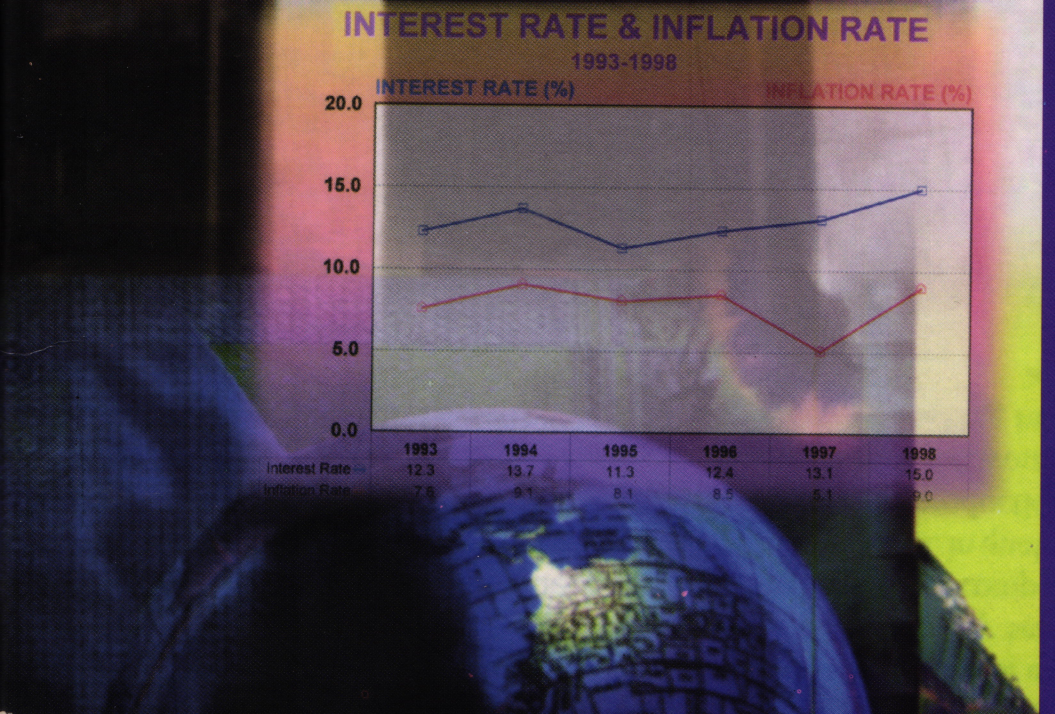
Republic of the Philippines
DEPARTMENT OF FINANCE

1998



ANNUAL REPORT

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DOF MANDATE

Under Excutive Orders 127, 127-A and 292, the Department of Finance is responsible for the following:

1. Formulation, institutionalization and administration of fiscal policies in coordination with other concerned subdivisions, agencies and instrumentalities of the government;

2. Generation and management of the financial resources of government;

3. Supervision of the revenue operations of all local government units;

4. Review, approval and management of all public sector debt, domestic or foreign; and

5. Rationalization, privatization and public accountability of corporations and assets owned, controlled or acquired by the government.

Letter to the President

His Excellency
JOSEPH E. ESTRADA
President
Republic of the Philippines
Malacañang, Manila

Dear Mr. President:

On behalf of the officials and employees of the Department of Finance, I am honored to submit to your Excellency the 1998 Annual Report of the Department.

The report reveals how the Department fulfilled its mandate with support from its bureaus, agencies and instrumentalities. We are pleased to note that despite our fiscal constraints, we were able to cushion the impact of the regional crisis on the Philippine economy.

Nonetheless, our commendable performance in 1998 was largely due to the strong leadership of Your Excellency even as the smooth transition to the country's Presidency happened during the year.

As we continue to face the challenges of our times, rest assured that the entire DOF family is behind Your Excellency in making the Philipines a better place for every Filipino as we enter a new millennium.

Very truly yours,

EDGARDO B. ESPIRITU
Secretary

Message from the President

Republic of the Philippines
Malacañang, Manila

For over a century, the Department of Finance has been mobilizing the country's financial resources as it continues to fulfill its role in nation building.

In 1998, we all felt the pain inflicted on us by a combination of forces, such as the financial crunch, the El Niño phenomenon and a series of calamities which deprived us of a more productive economy even as the country commemorated the centennial of its emergence as an independent republic.

The 0.1% GNP growth was the best the Philippine economy could deliver in 1998 in the face of these shocks. Indeed, it provided some small reason to celebrate as we were less affected by the financial crisis than most of the countries in the region.

Like most economies in Asia, we have not fully recovered from the bruises wrought by these factors. The prospects of uncertainties remain in the horizon, but compared with our neighbors we are still in a better position on the road to recovery.

Much of this can be attributed to the key structural reforms that are already in place and which shall continue to be deepened. The country was able to maintain manageable levels of deficits, inflation and interest rates, a sound banking system, a relatively stable currency and the continued confidence of the business community.

By and large, we achieved resiliency amidst crisis and we made it during the year when many Asian economies plunged into recession. As we march toward the 21st century, my greatest dream is to see the Philippine economy back on a sustainable growth path that allows us to erase poverty early in the next decade.

Rest assured that the Department of Finance remains at the forefront of economic reforms as it continues to enhance the country's revenue system.

Good luck and keep up the good work.

JOSEPH E. ESTRADA
President
Republic of the Philippines

Message from the Secretary

The financial crisis that hit the region in mid-1997 rendered a less ambitious economic programming in 1998. It was in 1998 when the adverse impact of the crisis was particularly apparent in the real sector of the Philippine economy as it was in the case of most economies in Asia.

Nevertheless, the country ended 1998 with positive developments. For instance, inflation was kept within a single-digit level of 9.0 percent, despite a severe drought in the first half of the year and floods and typhoons during the second half.

The bellwether 91-day weighted average interest rate (WAIR) on Treasury bills, which is the barometer of lending rates in the credit market, fell from a high of 19.1 percent in January 1998 to 13.4 percent by December of the same year. As a result, lending rates followed the trend and dropped from a peak of 21.1 percent to 17.3 percent during the reference period.

In 1998, the currency market was among the many sectors that were closely watched by the country's policymakers as well as investors. The peso bounced back from a low of P45-US$1 at the height of the crisis and settled at an average of P40.89 to the dollar by year-end. This was partly due to massive inflow of dollar remittances and the return of portfolio investments.

For its part, the Department responded to the Estrada Administration's call to stimulate the economy and immediately implemented an expansionary fiscal policy in the second half. This deficit financing strategy, however, was exercised with caution and attuned to the administration's priorities. The bulk of expenditures was channeled to agricultural modernization and expansion of rural infrastructure, the benefits of which might not have been felt in 1998, but will be reaped in the years ahead.

The year 1999 and beyond are predicted to be years of recovery. As I congratulate all officials and employees of the Department, I enjoin everybody to continue doing your best to help move the country forward.

EDGARDO B. ESPIRITU
Secretary

RESILIENCY AMIDST CRISIS

Recent Economic Developments

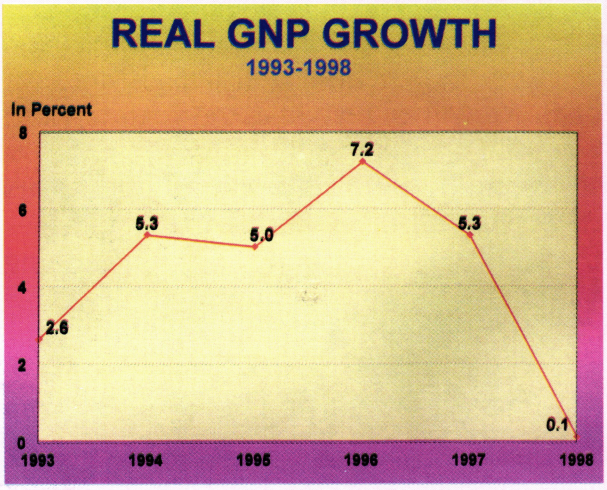
The year 1998 brought dramatic changes in both the regional and international economic environment. The crisis-affected Asian economies experienced drastic decline in output, a complete reversal from the robust growth they registered in the earlier part of the decade. In the Philippines, the lingering effects of the regional contagion and the twin weather disturbances - the El Niño and the La Niña phenomena - slowed down domestic economic activity. But the Philippines proved more resilient than its neighboring countries. It emerged as the only economy in the ASEAN excluding Singapore which recorded a positive economic growth in 1998.

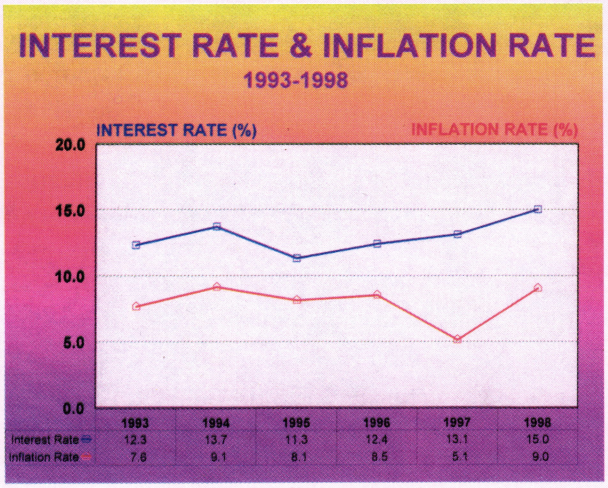
Real gross national product (GNP) grew by 0.1 percent in 1998 in contrast to 5.3 percent growth in 1997. The industry sector declined by 1.7 percent while agriculture contracted by 6.6 percent. The lackluster performance of agriculture was due to the adverse effects of the El Niño phenomenon in the first half and the La Niña - induced typhoons and floods in the second half. The services sector continued to buoy up the economy, expanding by 3.5 percent. On the other hand, the depreciation of the peso helped boost net factor income from abroad which grew by 12.9 percent.

Consumption was the principal source of output growth, accelerating by 3.5 percent as against the 5.0 percent growth registered in 1997. The imposition of mandatory budget reserves slowed down government consumption, posting only 0.8 percent increase in 1998 from 2.4 percent in 1997.

Prudent fiscal and monetary policies kept inflation within a single-digit level of 9.0 percent, using 1988 as base year, compared to the 5.1 percent inflation rate registered in the previous year. The higher inflation was caused by supply factors. A severe drought in the first half of the year, and floods and typhoons made stronger by La Niña in the last quarter of 1998 jacked up food prices which constitute the bulk of the consumer price index (CPI) basket.

The bellwether 91-day rate on Treasury bills, which is the barometer of lending rates in the credit market, fell from a high of 19.1 percent (WAIR) in January 1998 to 13.4 percent by December 1998. Lower lending rates followed the drop of T-bill rates from a peak of 21.1 percent in January 1998 to 17.3 percent as of December 1998. From the tight liquidity adopted to curb speculative attack on the peso in the few months, monetary





authorities shifted to relatively expansionary grade to encourage lending to economic activities and rekindle economic growth. Further, the increased preference by banks for more secure Treasury instruments during the second half pulled down the year-end average to 15.0 percent.

After being in deficit for years, the country's current account balance turned into a surplus of US$786 million in 1998 or equivalent to 1.2 percent of GNP. The marked improvement in the current account balance was due to the steady stream of dollar remittances by Overseas Filipino Workers (OFWs) and continued surge in exports. Moreover, the substantial decline in imports narrowed the gap in merchandise trade, further boosting the current account balance.

The regional financial crisis engendered speculative attacks on the peso along with other Asian and international currencies. From an average of P29.47 to the U.S. Dollar in 1997, the peso depreciated by 39 percent, breaching the P45-US$1 level at the height of the crisis. However, favorable developments in the international economic scene and the massive inflow of dollar remittances and of portfolio investments bolstered the peso during the last quarter. The peso settled at an average of P40.89 to the dollar by year-end.

On the fiscal front, the Government paved the way for quick economic recovery through the adoption of an expansionary fiscal stance. The bulk of expenditures was channeled to the modernization of agriculture and the expansion of rural infrastructure.

Even as it went into deficit financing, the Government exercised prudent expenditure management. This included the implementation of reforms on budget allocation and the deferment of the implementation of certain programs under the special purpose funds and subsidies to government corporations.

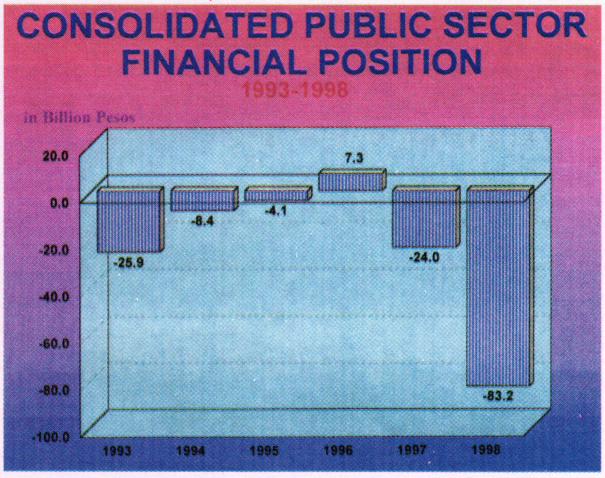
Overall, the Department made its contributions felt through the adoption of a fiscal stance that would support sustained growth. As revenue performance wavered at the height of the crisis, the Department undertook tax administration improvements to bolster collection efficiency.

With the economy slowing down, the Government supported the shift of fiscal stance in order to bolster growth, promote macroeconomic stability, induce higher productivity and strengthen the country's international competitiveness. Moreover, it advocated efforts toward further liberalization, deregulation and privatization.

FISCAL MANAGEMENT

Consolidated Public Sector Financial Position

In 1998, the Consolidated Public Sector Financial Position (CPSFP), which is the combined financial position of all government entities, incurred a deficit of P83.2 billion, from P24.1 billion in the previous year. The higher deficit was attributed mainly to the P50.0 billion deficit posted by the National Government due to its pump priming activities and the higher financing deficit of government-owned and controlled corporations (GOCCs)



because of the need to increase the buffer stock of rice.

RESOURCE MOBILIZATION

Amidst the economic downturn, the Department managed to generate revenues to finance government operations. In 1998, total revenues reached P462 billion, slightly lower than the P472 billion registered in 1997. The 18.4 percent decline in imports resulted in lower Bureau of Customs (BOC) collections. The higher receipts from internal revenue tax collections and fees and charges partially made up for the lower collections from other revenue sources.

To cover the deficit, the Department tapped local and foreign creditors for financing. In 1998, it raised P88 billion in net financing, of which P12 billion were raised from external sources and P76 billion from domestic sources.

Tax Revenues

In 1998, tax revenues reached P416 billion, or an increase of P4.0 billion over the P412 billion collected in the previous year. The Bureau of Internal Revenue (BIR) generated P337 billion. This was P23.0 billion or 7.0 percent higher than the collection recorded in 1997 but P17.9 billion below the target. The slowdown in the economy dampened tax collections.

The Bureau of Customs contributed P76 billion in duty collections in 1998 or a 20 percent decline from the P94 billion realized in 1997. The 18.4 percent decline in imports and the lower average tariff rates contributed largely to the shortfall in collection.

Non-Tax Revenues

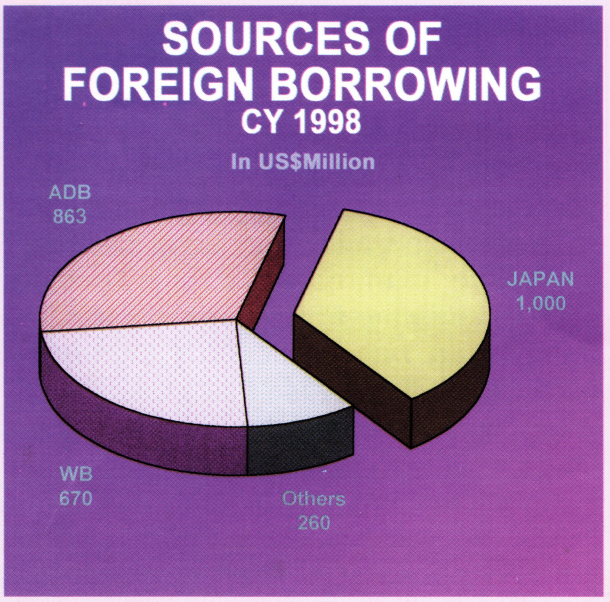
Non-tax revenue collection went down by 23 percent, from P59 billion in 1997 to P45 billion in 1998. This was largely due to lower privatization receipts which plunged to P1.7 billion from P9.4 billion in 1997. The substantial gains in income posted by the BTr and the higher receipts from fees and charges cushioned the decline in non-tax revenues.

Domestic Borrowing

Gross securities flotation of the National Government reached P569 billion in 1998. Treasury Bill offerings amounted to P498 billion as against P370 billion in 1997. To limit the impact of high interest rates which prevailed in the first quarter of the year and avoid being locked into high interest rate bonds, most of the Treasury Bill offering were concentrated on short-term securities. However, as interest rates declined, the BTr resumed the issuance of Treasury Bonds. Treasury bond flotation rose by only P3 billion, from P68 billion in 1997 to P71 billion in 1998.

Foreign Borrowing

In 1998, the Department secured 41 loan agreements totaling US$2.8 billion. The bulk of these loans came from Japan (US$1.0 billion or 36 percent of the total loans signed), the Asian Development Bank (US$863.8 million or 21 percent) and the World Bank ($670.8 million or 24 percent). Other creditors include the United States of America, Korea, Swedish International Development Agency, Canada, Australia, France, Austria and Kuwait Fund. These loans financed projects related to power restructuring, air quality improvement, financial reforms, agricultural and rural development, social services, health services and economic development in Special Zone of Peace and Development (SZOPAD) in Mindanao.



DEBT MANAGEMENT

The government maintains a strategy of optimizing domestic and foreign borrowings at the most concessional terms. In 1998, it tapped non-traditional sources of financing, opening new possibilities of alternative financing in the future. Debt indicators remained within prudent levels in spite of the financial crisis.

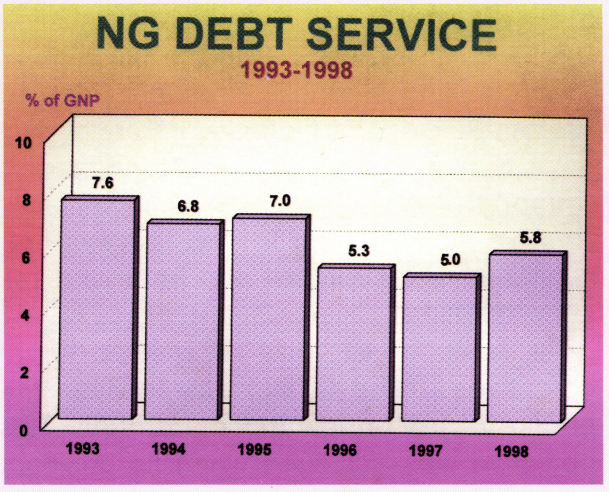
The National Government debt outstanding rose to P1,496.2 billion in 1998 from P1,388.6 billion in 1997. Despite the increase, the ratio of debt outstanding to GNP declined from 53.5 percent in 1997 to 49.8 percent in 1998. The National Government debt service as a percentage of GNP rose slightly from 5.0 percent to 5.8 percent. The higher debt service expense, which include principal payments and interest expense, resulted largely from the hike in interest rates and the peso depreciation.

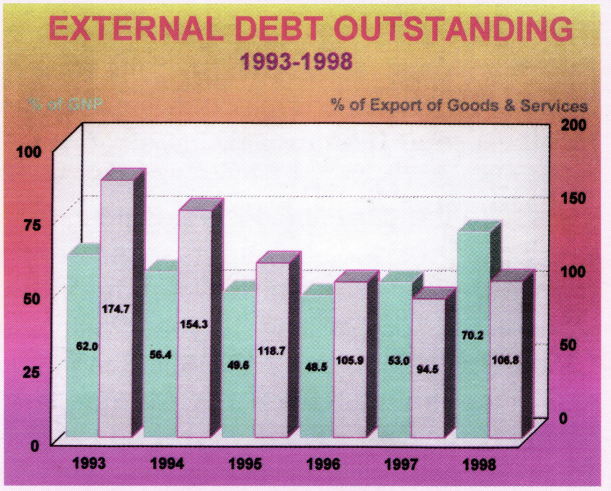
Domestic Debt

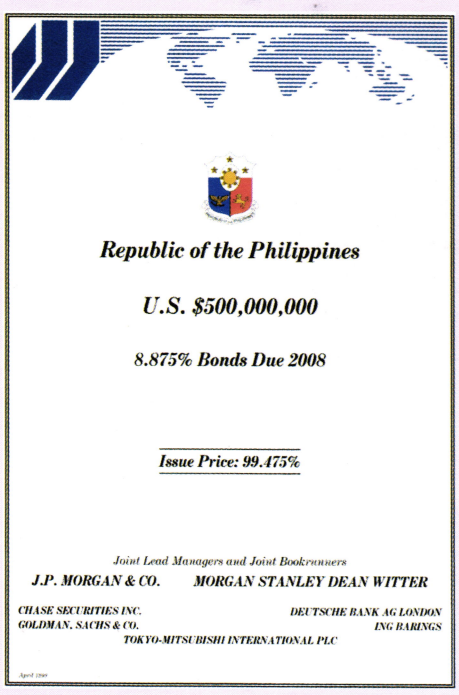
The National Government domestic debt reached P833 billion or an increase of 11.1 percent over the previous year's level of P749.7 billion. The National Government cut its weekly auction of Treasury bills to P5 billion as it tapped small investors by issuing small denomination Treasury Bills.

External Debt

The country's external debt outstanding reached US$47.9 billion, or 0.5 percent higher than the 1997 level of US$45.4 billion as a result of the peso depreciation and additional foreign loans by the government to shore up revenues and pump prime the economy.







A billboard fronting the Morgan Stanley Building in New York proclaims the launching of RP Global Bonds.

Buoyant export receipts allowed the ratio of external debt to exports of goods and services to stay at the manageable level of 106.8 percent.

Despite the currency crisis besetting Asia and poor investor sentiments in emerging markets, the Philippines successfully launched a $500 million 10-year Philippine Global Bonds last April 2, 1998. Managed by U.S. investment banks J.P. Morgan and Morgan Stanley, the bond was priced at 337.5 basis points above the 10-year U.S. Treasuries, more favorable than a similar issue by Brazil. The overwhelming reception resulted in oversubscription of the offering which actually reached $1 billion. The bonds were bought mostly by institutional investors from the U.S., Japan, Hongkong and Europe.

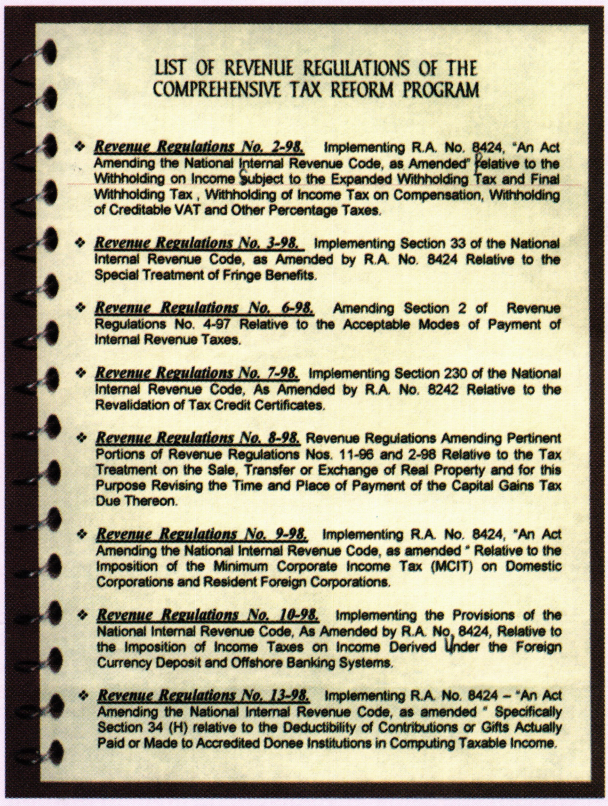
The favorable pricing and long maturity of the issue manifested strong investor confidence in the Philippine economy. The bond issue was particularly significant because: (1) it made the Philippines the first Asian country to access the voluntary markets after the currency turmoil erupted; (2) it raised a significant amount of resources from institutional investors, many of whom invested in the Philippines for the first time; (3) it opened up access by Philippine infrastructure projects to new sources of financing; and (4) it relieved pressure on domestic interest rates and boosted international reserves.

The National Government also tapped a bridge financing amounting to US$610 million.

UPDATE ON THE COMPREHENSIVE TAX REFORM PROGRAM

The passage of the three components of the Comprehensive Tax Reform Program (CTRP) -- Republic Act 8184 (Restructuring of the Excise Tax on Petroleum Products), Republic Act 8240 (Shift in the Taxation of Cigarette and Alcoholic Products from Ad Valorem Tax to Specific Tax) and Republic Act 8424 (Restructuring of the Individual and Corporate Income Tax) -- has significantly removed distortions in the tax system, simplified tax structure and improved tax administration.

As envisioned, one of the principal objectives of the CTRP was to ease the burden of tax on low income groups. This objective was achieved when its pro-poor



LIST OF REVENUE REGULATIONS OF THE COMPREHENSIVE TAX REFORM PROGRAM

- ***Revenue Regulations No. 2-98.*** Implementing R.A. No. 8424, "An Act Amending the National Internal Revenue Code, as Amended" Relative to the Withholding on Income Subject to the Expanded Withholding Tax and Final Withholding Tax , Withholding of Income Tax on Compensation, Withholding of Creditable VAT and Other Percentage Taxes.
- ***Revenue Regulations No. 3-98.*** Implementing Section 33 of the National Internal Revenue Code, as Amended by R.A. No. 8424 Relative to the Special Treatment of Fringe Benefits.
- ***Revenue Regulations No. 6-98.*** Amending Section 2 of Revenue Regulations No. 4-97 Relative to the Acceptable Modes of Payment of Internal Revenue Taxes.
- ***Revenue Regulations No. 7-98.*** Implementing Section 230 of the National Internal Revenue Code, As Amended by R.A. No. 8242 Relative to the Revalidation of Tax Credit Certificates.
- ***Revenue Regulations No. 8-98.*** Revenue Regulations Amending Pertinent Portions of Revenue Regulations Nos. 11-96 and 2-98 Relative to the Tax Treatment on the Sale, Transfer or Exchange of Real Property and for this Purpose Revising the Time and Place of Payment of the Capital Gains Tax Due Thereon.
- ***Revenue Regulations No. 9-98.*** Implementing R.A. No. 8424, "An Act Amending the National Internal Revenue Code, as amended " Relative to the Imposition of the Minimum Corporate Income Tax (MCIT) on Domestic Corporations and Resident Foreign Corporations.
- ***Revenue Regulations No. 10-98.*** Implementing the Provisions of the National Internal Revenue Code, As Amended by R.A. No. 8424, Relative to the Imposition of Income Taxes on Income Derived Under the Foreign Currency Deposit and Offshore Banking Systems.
- ***Revenue Regulations No. 13-98.*** Implementing R.A. No. 8424 – "An Act Amending the National Internal Revenue Code, as amended " Specifically Section 34 (H) relative to the Deductibility of Contributions or Gifts Actually Paid or Made to Accredited Donee Institutions in Computing Taxable Income.

provisions were finally put into effect in 1998. Taxpayers living below the poverty threshold of P60,000 are now exempted from the income tax. Individual taxpayers enjoyed increased personal and additional exemptions and lower marginal tax rates. A family of six, for instance, enjoys a maximum exemption of P98,400 and additional maximum deduction of P2,400 for health and/or hospitalization insurance. These resulted in lower tax burden for the majority of taxpayers.

On the other hand, the contribution of more affluent taxpayers to government coffers was enhanced with the introduction of the minimum corporate income tax, limits on deduction, imposition of a fringe benefit tax and taxation of interest income from FCDU deposits.

The restructuring of rates for petroleum products under RA 8184 increased collection from P16.4 billion in 1997 to P18.0 billion in 1998. The increase in the prices of oil along with higher consumption likewise contributed to substantial collection.

The implementation of the CTRP required the issuance of revenue regulations. Most of these regulations were issued and became effective in 1998. These regulations were promulgated to prescribe the procedures and guidelines in order to facilitate compliance with the CTRP.

THE GOVERNMENT CORPORATE SECTOR

Fiscal Performance of GOCCs

Heavy rice importations by the National Food Authority to bolster buffer stocks because of El Niño and La Niña increased the financing deficit of the thirteen major non-financial GOCCs to an estimated P38.0 billion in 1998 from P17.9 billion in 1997.

The surplus of the government financial institutions (GFIs) increased to P5.4 billion in 1998 compared with P4.4 billion registered in 1997 as they expanded their lending activities to offset the slack in private bank lending complemented by lower expenditure. The Social Security Institutions (SSIs) posted a P17.7 billion surplus, a substantial increase

GOVERNMENT CORPORATE SECTOR FISCAL POSITION

In Billion Pesos

	1997	1998	
	Actual	Program	Preliminary
GOCCs	-17.9	-26.2	-38.0
GFIs	4.4	4.8	5.4
SSIs	7.0	6.6	17.7
Total	-6.5	-14.8	-14.9

FISCAL POSITION OF 13 MAJOR NON-FINANCIAL GOVERNMENT CORPORATIONS

In Billion Pesos

	1997 Actual	1998 Program	1998 Preliminary
Total Receipts	117.8	161.5	147.0
Current Expenditures	99.9	155.3	141.0
Capital Expenditures	35.8	32.4	44.0
Internal Cash Generation	17.8	6.2	6.0
Financing Surplus/Deficit	(17.9)	(26.2)	(38.0)

from P7.0 billion in 1997, due to higher member contributions and higher share of investment in National Government securities.

Administrative Reforms

The Department continued to enhance financial discipline among government-owned and controlled corporations (GOCCs). On August 14, 1998, through the Department's initiative, President Estrada issued Administrative Order (AO) No. 10 entitled "Strengthening and Enhancing the Procedure for Setting the Annual Net Lending Program for GOCCs, and Guidelines for the Conversion of NG Advances, Including Interest on NG Advances into Equity and/or Subsidy to GOCCs." This AO provides mechanism for a more effective way of programming advances to GOCCs and well-defined guidelines for conversion of NG advances into equity or subsidy. It allows the imposition of a penalty charged on advances made by the NG as guarantor / direct borrower of the GOCCs without favorable endorsement from the DOF.

In 1998, the Department initiated policy guidelines intended to finetune the regulations on the remittance by GOCCs of the NG share in their earnings and profit. These include:

a. Department Circular Nos. 1-98 and 2-98 dated 12 August 1998, effecting the mode of remittance of the 50 percent NG shares from the Philippine Amusement and Gaming Corporation's (PAGCOR) gross earnings after franchise tax and 1.5 percent NG share from Duty Free Philippines' net sales.
b. Revised Implementing Rules and Regulations to Republic Act No. 7656 (Dividend Law) dated 05 August 1998. This is aimed at improving implementation and defining gray areas in the original Implementing Rules and Regulations to generate higher dividends from GOCCs.
c. Department Order No. 56-98 dated August 14, 1998 and Department Memorandum dated December 21, 1998. These enjoin local government units (LGUs), BIR, BOC, attached agencies of the DOF and all GOCCs to deposit and maintain cash balances with the government financial institutions (GFIs), namely, Land Bank of the Philippines (LBP), Development Bank of the Philippines (DBP), Philippine National Bank (PNB), Philippine Postal Savings Bank (PPSB) and rural and cooperative banks under certain conditions.

In consonance with the Administration's pro-poor policies, the Department likewise issued Department Order 57-98 on August 17, 1998 to induce private sector participation in lending to agriculture. This Order directed the review of charters and programs of the Agriculture Credit Policy Council (ACPC) and the government financial institutions - Land Bank of the Philippines, Philippine Crop Insurance Corporation, Guarantee Fund for Small and Medium Enterprises, and Quedan Corporation - in accordance with Rule 24 of the Implementing Rules and Regulations of R.A. 8435 (Agriculture and Fisheries Modernization Act). The review is intended to evaluate how well these institutions are able to provide the proper catalytic environment for private sector participation in credit for

agriculture.

The National Government, through DOF, likewise issued sovereign guarantee to various loans of GOCCs after a review and evaluation of the objectives for which the loans are to be incurred. Among these are the Countryside Loan Fund III, a $300M World Bank Loan conduited through LBP and DBP, which will expand existing regular lending programs to include credit for agriculture and industry; and the DM 15M loan from Kreditanstalt fur Weideraufbau (KFW) to finance the Small and Micro Enterprise Credit Project Phase 2 that will provide credit to finance fixed asset investment.

The DOF also extended support to the National Food Authority's (NFA) food security program and price stabilization functions through the grant of a sovereign guarantee on NFA's additional credit lines with various commercial banks amounting to P20.1 billion for its grains stabilization activities pursuant to the full powers and authority given by the President of the Philippines to the Department of Finance on December 4, 1998.

PUBLIC-PRIVATE SECTOR PARTNERSHIP

Privatization Program

Since its launching on December 8, 1986, the Philippine Privatization Program has achieved substantial progress. Aimed at stimulating investments and revenues for the National Government, the Committee on Privatization (COP) has privatized almost 80 percent of the government's assets and corporations identified for privatization. As of December 31, 1998, total cumulative revenues generated from privatization and divestment of asset/corporations have amounted to P185.2 as shown below.

Accounts	No. of Accounts	Total Proceeds (In Billion Pesos)
APT	343	44.6
PCGG	11	25
GOCCs	99	75.4
BCDA	1	39.2
Other Assets	1	1
Total	455	185.2

In 1998, the privatization program added P1.7 Billion to National Government coffers.

The privatization of GOCCs had the highest contribution to the proceeds with P75.4 billion, followed by transferred assets under APT (P44.6 billion), BCDA (P39.2 billion), PCGG (P25.0 billion) and other assets (P1.0 billion).

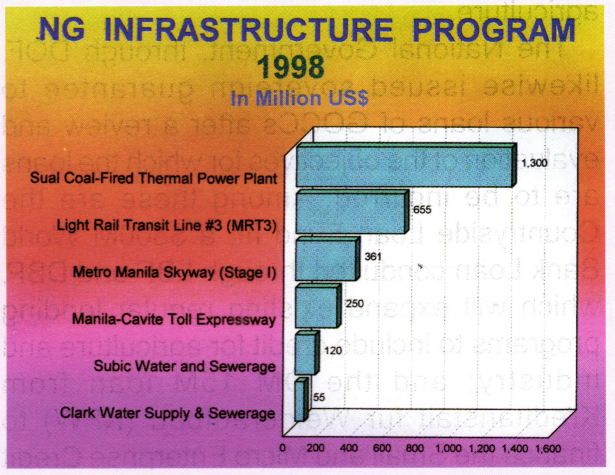
In 1998, privatization proceeds remitted to the National Treasury amounted to P1.7 billion, marking a total of P115.9 billion privatization remittances to the National Government from 1987 to December 31, 1998. The bulk of the remittances came from the PCGG's sale of surrendered shares of stocks of the California Overseas Bank and the Security Bank and Trust Company (P1.2 Billion). These proceeds, including interests, were previously deposited in escrow.

The first wave of privatization has been largely completed. The remaining big-ticket items for privatization include Food Terminal Inc., PNOC Energy Development Corp., PASAR and Philphos. In 1998, the privatization plan for PASAR was approved by the President. The government has already hired a consortium of banks to act as its financial advisor for the sale of its remaining equity at the Philippine National Bank (PNB).

The Build-Operate-Transfer (BOT) Program

The BOT Program was borne out of the critical need to address the power crisis in the early 1990s. With limited public resources, the government encouraged private sector investment initially in power generation projects. With its success, the Program has since been expanded to include extensive investment opportunities in tele-communications, tollways and mass transportation, water supply and treatment, and several other infrastructure areas. The involvement of the private sector in the Program was made more attractive through government and institutional support, fiscal incentives, credit enhancement and technical support through the CCPAP-BOT Center.

In 1998, the infrastructure program was heavily concentrated on power generation, tollways and mass transportation, and water supply and treatment. These include the Sual Coal-Fired Thermal Power Plant worth US$1.3 billion, Light Rail Transit Line No. 3 (MRT 3) estimated at US$655 million, Metro Manila Skyway (Stage 1) valued at US$361 million, Manila-Cavite Toll Expressway with projected cost of US$250 million, Subic Water and Sewerage worth US$120 million, and Clark Water Supply and Sewerage with estimated cost of US$55 million.



Metro Manila Skyway Stage 1

Malitbog-Mahanagdong, Tongonan Geothermal Power Plant

Similarly, the Department extended support to two vital infrastructure projects, namely, the Camago-Malampaya Natural Gas Project and the Non-Power Component of National Power Corporation's (NPC) Multi-Purpose Project. In the former, the government issued a Performance Undertaking on NPC's gas sale and purchase agreement with Shell-Oxy in recognition of the macroeconomic benefits derived from the project. In the latter case, the DOF issued sovereign guarantee in the amount of US$400 million Japan Eximbank loan to develop the Agno River for power generation, irrigation, flood control and water quality improvement.

CAPITAL MARKET DEVELOPMENT

Key reforms for capital market development continued to accelerate. The core reforms - full disclosure philosophy and the concept of

self-regulation -- are now in place in the administrative operations of the Securities and Exchange Commission (SEC). Under the full disclosure rules, all material and necessary information about the issuer of securities are disclosed in order to protect the interest of investors. On June 29, 1998, the Philippine Stock Exchange (PSE) was conferred permanent self-regulatory organization (SRO) status.

In 1998, administrative rules affecting securities markets were issued to ensure investor protection and to institute market discipline and accountability. These rules include requiring all stock brokers to submit their list of customers under oath to serve as basis in formulating policies towards wider distribution of allocated stocks in initial public offerings, and the implementing guidelines of Republic Act No. 8366 (Philippine Investment House Industry Act) with respect to the reciprocity requirement on foreign equity applications in investment houses and capital build-up requirements.

To complement the legislative reforms being undertaken are projects to support capital market development. These include the creation of the secondary bond market in the Philippines and the expansion of small investors base. In November 1998, the Bureau of the Treasury launched the Small Investor Program (SIP) to expand the investor base in government securities.

An equally important reform is the development of asset-backed securities (ABS) intended to enhance liquidity in the housing, consumer and infrastructure finance sectors.

President Joseph E. Estrada registers as first investor in the Small Investors Program (SIP) launched by the Bureau of the Treasury on November 5, 1998. Looking on are DOF Secretary Edgardo B. Espiritu, National Treasurer Leonor M. Briones and representative from government and private sectors.

The insurance sector expanded with the liberalization of the industry. In 1998, two (2) new life and one (1) non-life insurance companies were issued licenses, bringing the number of insurance firms operating in the country to 13 since the government liberalized the insurance sector in 1992.

The next phase of the tax reform process will focus on capital market development. The DOF began a review of the taxation of the financial sector by convening nine task forces with membership from industry and government. The task forces are working to establish the parameters of the reform, determine the structure and formulate a final package of proposed legislation for submission to Congress.

Specifically, the financial sector reform envisions a tax system that will promote neutrality and fairness across competing financial institutions and instruments. The Department believes that taxes should not distort investment decisions. Secondly, a level playing field in the financial sector encourages savings and the development and trading of financial instruments. Lastly, the reforms should ensure that the financial sector bears an equitable share in the total tax burden.

Small Investor Program

On November 5, 1998, the government, through the Bureau of the Treasury, launched the Small Investor Program (SIP). The SIP is intended to tap a wider marker for government securities to include small savers and ordinary households. The rationale behind the Program is that small, untapped savings, once pooled and mobilized, can be instrumental in further enhancing the capital market.

Housing Finance

Housing is a major priority concern of the Estrada administration. In support of this priority area, the Department is spearheading the generation of resources for the housing sector, and is working closely with the Housing and Urban Development Coordinating Council in developing reforms to make housing finance more sustainable.

The strategy for reform includes the strengthening of the guarantee system for shelter finance, introducing market-based pricing structures to encourage more private sector lending in the housing sector, and improving the policy and regulatory framework for asset-backed securities.

In 1998, the Department initiated steps to increase the guarantee capability of the Home Insurance Guaranty Corp. (HIGC) to enable it to underwrite more socialized housing projects. The approach being studied for this purpose is not the usual capital infusion through budgetary outlays, but rather the assignment to HIGC of idle government properties.

To unleash the potential of securitization as a major alternative source of financing, the Department initiated the following activities:

- Rationalizing the taxation of asset-backed securities to level the playing field between them and other securities traded locally;
- Ensuring clear and consistent regulatory treatment by the Bangko Sentral, the Securities and Exchange Commission and the Insurance Commission;
- Improving and facilitating the approval process and supervision of asset-backed securities; and
- Improving the environment for new types of securitized products.

By reforming the policy and regulatory framework for securitization, it is hoped that the private sector will be encouraged to launch more securitization projects which will redound to greater liquidity for housing and real estate development finance.

Government policy will be based on a two-pillar approach. The first pillar is the move towards market-based financing to increase the liquidity and soundness of portfolio in a

competitive housing finance industry. The second pillar provides for transparent and budgeted transfers for the lower 30 percentile of the population who cannot afford loans and market rates.

To strengthen the implementation of these two approaches, the Department is reviewing the existing legal, regulatory, tax and infrastructure framework. This is critical for the development of a secondary market for mortgaged-backed securities (MBS) in the Philippines. Once developed, the MBS would increase the availability of mortgage financing which in turn would decrease cost, accelerate the development of the capital market and broaden alternatives available to banks to reduce the risks associated with property lending.

LOCAL GOVERNMENT FINANCE

The devolution of more powers and resources to local government units (LGUs) under the Local Government Code of 1991 has allowed LGUs greater leeway to grow in the direction they have set for themselves and according to their own capabilities. With greater fiscal autonomy, local officials have been able to provide and deliver services according to their needs and preferences.

The DOF, through the Bureau of Local Government Finance (BLGF), in collaboration with the BOT Center, is promoting a new financing paradigm to improve the fund sourcing capability of LGUs. The BLGF has prepared an action program that would open LGU access to private sector financing of local government services and infrastructure. Regional seminars on credit financing and BOT arrangements and other forms of private sector participation were staged nationwide informing LGU officials of various sources of financing such as loans, bonds, BOT and its derivatives and other joint venture programs.

The Municipal Development Fund (MDF)

The Municipal Development Fund (MDF), established in 1984 by virtue of P.D. 1914 to operate as a revolving fund, continues to provide financing to LGU development projects. A total of 126 LGUs has availed of funds for infrastructure and economic enterprises, while some 850 LGUs were given grants to improve real property tax administration (RPTA). As of December 1998, cumulative receipts of development project funds for MDF amounted to P11.6 billion.

Executive Order No. 41 issued on November 20, 1998 further strengthened the role of MDF by creating the Municipal Development Fund Office (MDFO) under the DOF.

The MDFO, when fully operationalized, shall perform the following:

- Act as a source of credit finance in support of decentralization of services from the national to the local levels of government;
- Promote the acceptability of borrowing as a means of financing a wide range of local government investment;
- Promote and assist local governments in the selection of well-justified and high-quality investments in infrastructure projects and public utilities; and
- Encourage a cost-recovery approach to the provision of suitable public services through the levy of appropriate levels of fees and user's charges.

The MDF is being restructured to enhance its role in helping poorer LGUs build a track record of creditworthiness and the capabilities for financial planning and project management. This way, there will be more access by LGUs to official development assistance (ODA) and private sources of capital.

The LOGOFIND Project

The Local Government Finance and Development (LOGOFIND) is a DOF project aimed at providing long term credit financing and technical support to LGUs through the MDF. The project is funded by the World Bank and has the following objectives:

- To assist LGUs in expanding and upgrading basic municipal and urban infrastructure, services and facilities by making available financial assistance in the forms of loans and grants; and
- To strengthen LGU capabilities in municipal investment and development planning, revenue administration, and project preparation and implementation by extending technical assistance and through a capability building program that is responsive to the needs of the LGUs.

The main target beneficiaries of the Project are low-income LGUs. It follows the demand-driven approach by which LGUs will be given a choice of sub-projects that are eligible for LOGOFIND financing.

The Community Based Resource Management Project (CBRMP)

The Community Based Resource Management Project (CBRMP) is aimed at reducing rural poverty and environmental degradation through support for locally generated and implemented natural resource management projects.

The overall objective of the project would be met several ways:

- Enhancing the capacity of low-income rural local government units (LGUs) and communities to plan, implement and sustain priority natural resources management projects;
- Strengthening higher levels of government system to transfer finance and environment technology, and improve implementation of environmental policies; and
- Providing resources to LGUs to finance natural resources management projects.

DOF AND SOCIAL REFORM AGENDA

The Department continues to be the champion of the National Government credit policy framework. The Department utilizes the inter-agency National Credit Council (NCC) as a forum to formulate and generate credit and savings policies to alleviate the plight of the marginalized sectors of society.

National Credit Council

For the year 1998, through its USAID-funded Credit Policy Improvement Program (CPIP), the NCC completed ten (10) studies that would help rationalize government credit programs and strengthen government credit policy. Eight (8) of the studies were published as Policy Notes and were distributed to various stakeholders. These studies include a review of directed or mandated credit programs of the government, interest rate subsidies, microfinancing for the poor, loan guarantee programs and microlending, among others.

To ensure advocacy of government credit policies, the NCC actively participated in the formulation of the Implementing Rules and Regulations (IRR) of the credit provisions of the "Agriculture and Fisheries Modernization Act (Republic Act No. 8435) and the "Social Reform and Poverty Alleviation Act" (Republic Act No. 8425).

The National Strategy for Microfinance which was drafted in 1997 was presented to the Donor's Working Group of Poverty Alleviation on March 9, 1998. The Strategy served as the basis of information for donors before committing funds for poverty alleviation. The meeting was facilitated

The National Credit Council

through the Consultative Group Secretariat (World Bank). The Strategy was likewise presented to the Second Annual Micro-Credit Summit in New York on June 24-26, 1998.

To ensure a seamless transition into the new administration, the NCC convened a planning conference of its member agencies. The conference laid down the priority activities of the NCC for 1998 and 1999 and undertook a review of the USAID-funded CPIP project. In addition, measures relative to the rationalization mandate of the NCC were discussed and the revised set of credit policies was approved in principle. The NCC decided to formulate the framework for the government's credit policy through an executive order (EO). The EO will enshrine an objective, market-oriented credit policy framework. The draft EO has been presented to the different Cabinet Clusters for comments and endorsement to the President for his signature.

In September 1998, the Technical Board of the Investment Coordinating Committee (ICC) started requiring NCC endorsement of the on-lending terms of proposed foreign loans and project proposals with credit component before it could be presented to the ICC Cabinet. As of December 31, 1998, six (6) project proposals have been reviewed and endorsed by the NCC. Strengthened coordination between NCC and ICC fulfills the objective of rationalizing and optimizing the use and delivery of government credit programs.

The NCC, in coordination with the Agricultural Credit and Policy Council (ACPC), initiated the drafting of the design of the Agro-Modernization Credit and Financing Program (AMCFP). Prior to the approval of the AMCFP,

regional multi-sectoral consultation workshops were conducted in Davao and Southern Luzon in December 1998. The AMCFP paves the way for a more rational credit implementation for the agricultural sector.

The Department, as the NCC Secretariat, continued its advocacy on government credit policy, principally during the Policy Advisory Group of Meetings of the Microfinance Coalition for Standard and Microstar Advisory Board; National Economic Summit; National Microcredit Summit; Workshop on Social Development; Meetings of the Investment Coordinating Committee Technical Board (ICC-TB); People's Credit and Finance Corporation (PCFC) Board Meetings; Workshops with the Basic Sector; Foundation for Sustainable Society, Inc. (FSSI) Board Meetings; and Briefing on the NCC to the newly appointed heads of the various NCC member-agencies.

INTERNATIONAL INITIATIVES

DOF and APEC

On May 23-24, 1998, the Asia-Pacific Economic Cooperation Ministers met in Kananaskis, Canada to assess future prospects for growth and development within the region in light of the Asian crisis and to discuss policies and measures to improve such prospects. The meeting focused on two broad themes. First was an assessment of the current economic situation and policies to restore financial stability and growth, including measures to strengthen social safety nets to help cushion the impact of the crisis on the poor. Second was the development and strengthening of financial markets in the region to reduce the likelihood of future financial instability and to facilitate the continued dynamic growth of the region. The Department supported the Ministers' call for a continuing dialogue and more concerted approach to solving the crisis.

DOF and ASEAN

1. ASEAN Post Ministerial Conferences

The Department participated in the 31st ASEAN Post Ministerial Conferences held in Manila last July 28-29, 1998. During the meeting, ministers from ASEAN and ten dialogue partner countries discussed the financial and economic situation in Asia and its repercussions on growth, employment and poverty. The conference noted that, unless the crisis was resolved, regional peace and stability would be undermined, creating an impact on global prosperity.

2. ASEAN Summit

The Department participated in the 6th ASEAN Summit held in Hanoi, Vietnam last December 15-16, 1998. The meeting produced three agreements that would hasten economic integration among member countries. These agreements are : (1) Framework Agreement on Mutual Recognition Arrangements, (2) Framework Arrangement on the Facilitation of Goods and Services, and (3) Implementation of the Second Package of Commitments under the ASEAN Framework Agreement Services.

Pursuing the Manila Framework

Since its inception in November 1997, the Manila Framework has become a historic document. It has fostered closer cooperation among APEC economies through a concerted and unified approach in addressing economic problems in the region. The Framework is constantly referred to in various international fora for discussing the Asian crisis.

The Framework recognizes the central role of the IMF in the international monetary system and includes the following initiatives: (a) a mechanism for regional surveillance to complement the global surveillance by the IMF; (b) enhanced economic and technical cooperation, particularly in strengthening domestic financial system and regulatory capacities; (c) measures to strengthen the IMF's capacity to respond to financial crisis; and (d) a cooperative financing arrangement that would supplement the resources of the IMF and other international financial institutions.

In 1998, the Department attended the following international meetings and discussions to promote the objectives of the Manila Framework:

- 2nd ASEAN Finance Ministers Meeting (February 28, 1998, Jakarta, Indonesia). During the meeting, finance ministers supported the proposal for the immediate establishment of the ASEAN surveillance mechanism with the assistance of the Asian Development Bank (ADB). They supported the Philippines' call for G7 countries to open their markets further to products from ASEAN and to adopt a more proactive approach to overcoming the currency crisis.
- The 2nd Manila Framework Deputies Meeting (March 26-27, 1998, Tokyo Japan). The Meeting reviewed the progress in addressing the currency crisis and preparing the groundwork for sustainable growth. The Deputies supported the Philippines' intervention to recognize the importance of resolving the critical private sector debt problem in Indonesia. It was agreed that the Manila Framework provided a useful forum through which frank and open discussion could provide mutual surveillance in maintaining sound economic and financial policies;
- G-7 Manila Framework Deputies Meeting (June 20, 1998 Tokyo, Japan). The Meeting focused on the economic and financial situation across the region. The Deputies agreed on the Philippines' intervention to recognize the commitment of China not to devalue its currency as a stabilizing factor in the region. The Philippines echoed the Deputies' call for the Japanese government to address its financial problems as swiftly as possible.
- ASEAN Senior Finance Officials Meeting (July 4-5, 1998 Yangon, Myanmar). The creation of an ASEAN surveillance mechanism that was proposed by the Department during the ASEAN Finance Ministers Meeting on December 1, 1997 came closer to reality when the members of the working group agreed on the following principles for the establishment of the ASEAN Surveillance Mechanism. That the Surveillance Mechanism should be informal, simple and built upon Article IV Consultation with the IMF; That the surveillance exercise shall be based on peer review process; and that the ASEAN Central Bank Forum shall contribute its finding to the surveillance process through the ASEAN Select Committee.
- ASEAN Select Committee Meeting (September 7, 1998, Kuala, Lumpur, Malaysia). The meeting agreed to recommend to the ASEAN Finance Ministers the Terms of Understanding for the establishment of the ASEAN Surveillance Process. During the meeting, participants agreed to adopt the Philippine position on the following: (1) establishment of an ASEAN Surveillance Technical Support Unit (ASTSU) at the ADB Headquarters in Manila, (2) the ASTSU would be comprised of seconded officials from member countries supported by ADB counterpart staff. The Philippines will second one staff to the ASTSU, and (3) a Philippine senior official would oversee the functions of ASTSU on a day-to-day basis.

Finance and tax officials from 16 APEC economies and 13 OECD member countries pose for posterity with DOF and BIR personnel during the 2nd APEC-OECD Symposium on International Business Taxation on November 4-6, 1998 in Cebu City

The 2nd APEC-OECD Symposium on International Business Taxation

The Department of Finance hosted the 2nd APEC-OECD Symposium on International Business Taxation held in Mactan, Cebu on November 4-6, 1998. The Symposium brought together senior finance and tax officials from sixteen APEC economies and thirteen OECD-member countries, as well as the IMF. The primary objective of the Symposium was to determine the impact of globalization on tax policy and administration in APEC and OECD countries. In particular, the Cebu Symposium focused on electronic commerce for tax policy and administration, harmful tax competition, tax implications of financial instability, access to information for tax administration, and taxation of multinational enterprises.

The meeting concluded with the agreement that a continuing dialogue on the areas discussed will be undertaken as participants agreed that global tax challenges require global cooperation so that individual country policy responses will be internationally consistent.

DOF FRONTLINE OFFICES

The Revenue Operations Group (ROG)

The Revenue Operations Group conducts careful review and monitoring of tax and duty exemptions granted to various sectors by the government. In 1998, the Revenue Operations Group - Customs and Tariff, Revenue Express Lane and Internal Revenue

Divisions - granted a total of P10.9 billion in tax and duty exemptions. This figure was higher than the P3.9 billion tax and duty exemptions granted in 1997. The steep increase in taxes and duties waived was accounted for by higher exemptions granted to NAPOCOR and Bangko Sentral ng Pilipinas (BSP). NAPOCOR's exemption reached P4.2 billion in 1998, from P554.7 million in 1997. Taxes waived for BSP amounted to P687.3 million in 1998, from P76.2 million in 1997.

The Mabuhay Lane

In 1998, the Mabuhay Lane granted a total of P9.5 billion in tax and duty exemptions. This figure was substantially lower than the 1997 figure of P14.7 billion. The drop in taxes and duties waived was mainly attributed to the expiration of Republic Act 7369 (Fiscal Incentives Law) on December 31, 1997, lower tariff rates on imports and the decline in the value of importation due to the currency crisis. The non-extension of the incentives enables the Department to reduce the negative impact of tax incentives on revenue collection.

One Stop Shop Inter-Agency Tax Credit and Duty Drawback Center

The One-Stop Shop Inter-Agency Tax Credit and Duty Drawback Center (CENTER) continued to administer the grant of fiscal incentives in the form of tax credits and duty drawbacks to exporters. To foster greater transparency in its operations, the CENTER initiated reforms towards the second half of 1998. Additional documents like the submission of financial statements were required in the filing of application. Audit and post-audit were conducted by an inter-agency team prior to and after the release of tax credits.

The reforms that were instituted substantially reduced the monthly average value of Tax Debit Memos (TDMs) issued from P526.8 million over the last two years to P394.7 million in 1998. On the other hand, Tax Credit Certificates (TCCs) released substantially dropped from P675 million in 1997 to P314.6 million in 1998.

The CENTER's thrust for the future will be the computerization of applications for tax credits, particularly the verification process to ensure faster and more effective processing. Grants are being tapped to ensure swift implementation. Moreover, the CENTER will establish the Audit and Verification Group as mandated under its charter to look after the veracity of tax credit claims.

HUMAN RESOURCE DEVELOPMENT

In celebration of the centennial of Philippine independence, the DOF established its own chapter of the Philippine Centennial Movement. The DOF Chapter included its bureaus and attached agencies. It actively participated in the International Congress of Women held in December 1998 at the Manila Midtown Hotel.

The Department recognizes that a well-motivated and highly trained personnel core is crucial to the effective performance of its role as fiscal manager of the economy. In 1998, the Department sent staff to attend regional courses and seminars sponsored by international agencies that focused on the Asian financial crisis like the IMF-sponsored courses on fiscal and monetary policy. These enabled the Department to have a better understanding of current issues as well as afforded the opportunity to highlight the structural reforms that the Philippines have already put in place.

Despite budgetary constraints, the Department continued to send employees to regular training programs here and abroad to

Delegates from the Department of Finance uphold women's agenda as they join the Women's Day Celebration held on March 6, 1998.

enhance their knowledge and skills on human resource management, accounting, auditing and budgeting, statistics, financial and records management, medical and dental care / treatment, fiscal and monetary policy, and supervisory and middle management courses.

The Department likewise raised the quality of human resource recruited into its fold by subscribing to the Brightest for the Bureaucracy Program (BBP) of the Civil Service Commission in the recruitment of highly competent young graduates. A number of them have been recruited for placement in various technical and administrative positions of the Department.

THE DOF MANAGEMENT TEAM

On July 1, 1998, the DOF family welcomed its new management team headed by Edgardo B. Espiritu as Secretary of Finance.

Secretary Espiritu brings to the DOF his vast experience in law, banking and finance. He is a Bachelor of Laws graduate from the University of the Philippines and in 1994 was the Awardee of the UP Law Alumni Association for his outstanding performance in the field of banking.

Three new undersecretaries strengthen the DOF team. Together with incumbent Undersecretary Milwida M. Guevara,

Secretary Edgardo B. Espiritu (2nd from right) heads the new management team (from left) Undersecretary Solomon S. Cua, Undersecretary Joel A. Bañares and Undersecretary Lily K. Gruba. Undersecretary Rodrigo P.Castelo joined the team on June 18, 1999.

Undersecretaries Joel A. Bañares, Solomon S. Cua, and Lily K. Gruba form the pillars of policy formulation as technical experts in economics, taxation, international finance, and law. Their combined knowledge, expertise, experience, and integrity buttress the formidable position of the DOF as premier economic agency.

Undersecretary Joel A. Bañares has a Masters of Business Administration degree from the Wharton School of the University of Pennsylvania and is a BS Business Economics graduate from the University of the Philippines. Undersecretary Bañares enhances the DOF policy team with his strong background in finance and banking and capital markets.

Undersecretary Solomon S. Cua is a Master of Laws from the London School of Economics and Political Science, University of London. He also holds a Bachelor of Arts in Mathematical Sciences and Economics from the University of Melbourne. Before joining DOF, Undersecretary Cua's background and work experience were in the fields of law, banking, real estate and manufacturing.

Undersecretary Lily K. Gruba obtained her law degree from the Ateneo de Manila University and earned her Master of Laws from the Georgetown School of Law, University of Georgetown. She has previously worked as Vice President, Special Assistant and General Counsel of the Land Bank of the Philippines. She joins DOF after years of practice as a lawyer.

ACCOMPLISHMENTS OF ATTACHED AGENCIES AND CORPORATIONS

Bureau of Internal Revenue

Total collections of the Bureau for 1998 amounted to P337.2 billion which was 7.1 percent or P22.5 billion higher than the previous year's collection of P314.7 billion. The collection, however, fell short of the goal by about 5.0% as the economy slowed down because of the serious weather disturbances and the Asian financial crisis.

During the year, the Bureau pursued administrative reforms and measures that would enhance revenue collection performance and ease tax administration, the foremost of which was the establishment of Large Taxpayers Unit (LTU) to monitor the tax payments of large corporations and conduct tax audits when necessary. The Bureau likewise intensified its tax mapping operations and the conduct of the Taxpayer's Record Update (TRU) Program on a nationwide scale in order to broaden the taxpayer base. As of December 31, 1998, registered taxpayers under TRU-Phase I (Taxpayers engaged in business) and TRU-Phase II totalled 473,278 and 2,181,570, respectively.

Legal and enforcement measures were also undertaken by the Bureau during the year. These include the disallowance of the use of tax credit certificates as payment for excise taxes by oil companies, identification of aliens evading payment of current taxes, audit of banks and insurance companies relative to their payment of documentary stamp taxes, and creation of Special Audit Team to audit conglomerates and interrelated group of companies.

The Bureau is undergoing sweeping organizational changes. It has submitted to the DOF a proposed organizational structure that emphasizes delivery of quality taxpayer services and strengthening core operational functions such as collections, assessment and enforcement.

Bureau of Customs

Despite the lower volume of importations arising from the Asian crisis and lower tariff rates, the Bureau of Customs managed to collect P76.0 billion in customs duties and taxes. This figure was lower than the P94.8 billion collected in 1997. Customs duties on oil and non-oil importations accounted for 57 percent on the year's cash collections, with VAT and excise taxes contributing 42 percent. Tax expenditure fund, which are actual payments on government importations, accounted for less than 1 percent.

The year 1998 was significant for the BOC computerization project. The Management Information System and Technology Group (MISTG) was organized to oversee the Bureau's management information system as well as strengthen its computerization program. The BOC's modernization program is also a timely response to the ever increasing need to facilitate trade in a world where economies are rapidly turning global as well as technologically more advanced.

The BOC launched and implemented the Direct Traders Input for remote entry lodgement and the BOC Electronic Date Interchange (EDI) Gateway to cater to warehousing entry lodgement. In a very short period of time, the computerization project has made headway in the BOC's effort to achieve a paperless, cashless and queueless transaction process between the Bureau and its partners in the business community.

Bureau of the Treasury

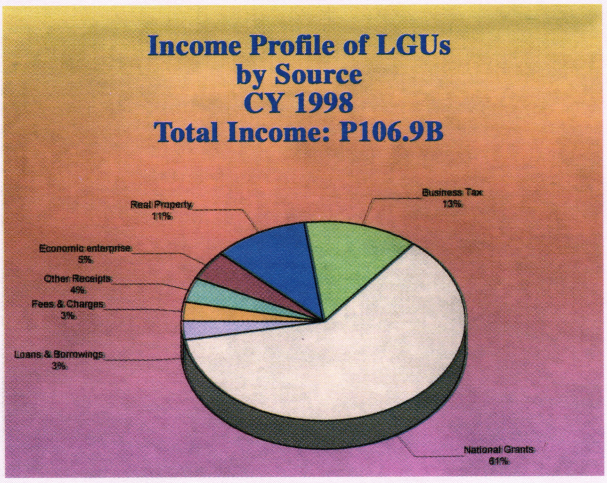
As of December 31, 1998, the outstanding cash balance in the custody of the Bureau amounted to P75.9 billion, lower than the

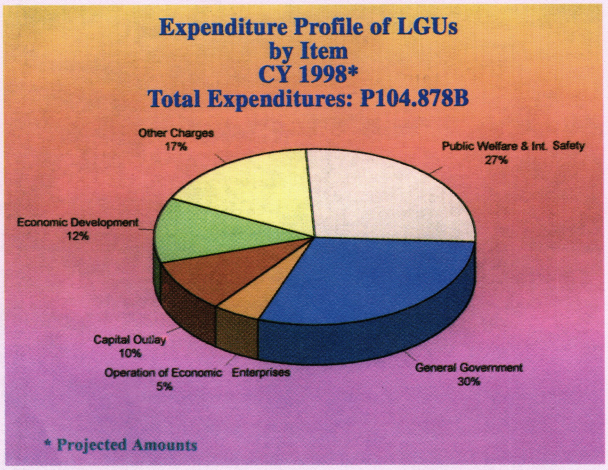
P93.0 billion registered in 1997. The lower cash balance was attributed to higher National Government withdrawals to finance increased funding requirements in line with the Government's pump priming policy and to minimize interest expense.

A significant achievement of the Bureau was the launching of the Small Investors Program (SIP) on November 5, 1998. The Program has enabled small savers to invest in government securities. As of December 31, 1998 there were 169 SIP ROSS Accounts opened for a total investment of P8.7 million.

Bureau of Local Government Finance

As the DOF's arm principally responsible for the enhancement and supervision of LGUs' financial operations, the Bureau of Local Government Finance (BLGF) continues to perform a catalytic role in bringing developmental changes to the local government sector. For CY 1998, it continued to pursue its thrusts towards skills development and capacity building for local assessment and treasury personnel, formulation of policies for the promotion of local fiscal autonomy, clarification of issues on local taxation, real property valuation and related local revenue matters, easier and wider LGU access to credit financing, and enhancement of local developmental pursuits.





With the real property tax being the main source of local government revenue, the continued implementation of the Real Property Tax Administration Project (RPTA) afforded the DOF, through the BLGF, the logistics to assume a larger and more proactive role in the provision of responsive and efficient property tax administration machinery. The Local Development Assistance Program (LDAP) has been completed, covering around 63.5 percent of the entire country or some 1,033 LGUs. The continuous monitoring of the financing performance of LGUs indicated that the collection of real property tax is likely to exceed the targets for 1998. As of November 1998, the collection effort of local treasury and assessment offices registered a total collection of P12.9 billion or 90.1 percent of the target of P14.3 billion.

Economic Intelligence and Investigation Bureau

The Economic Intelligence and Investigation Bureau (EIIB) safeguards government coffers against all forms of economic subversion and protects the environment against wanton degradation. The agency's intensified apprehension and seizure activities registered P363.6 million in additional revenues, while assistance in

internal revenue collection and environmental protection netted P4.5 billion.

Among the highlights of the Bureau's accomplishments for 1998 include the conviction of thirty four (34) illegal fishermen in violation of Presidential Decree 704. In the campaign against all forms of economic crimes, there were three (3) convictions for violation of Presidential Decree 1602 (Illegal Gambling Law). In August 1998, the Bureau launched an intensified campaign against sugar smuggling. These accomplishments were the results of one thousand two hundred seventy six (1,276) items of information gathered and evaluated. From the total, eight hundred seventeen (817) resulted in positive operations and/or investigations, three hundred twenty eight (328) were disseminated to other agencies while the rest remain for further build-up.

Securities and Exchange Commission

In 1998, the Securities and Exchange Commission (SEC) enhanced its regulatory function in the implementation of various capital market laws. The SEC remains vigilant in the performance of its task as overseer of the securities market and the corporate sector. It continued to adhere to the twin principles of full disclosure and self-regulation in developing the capital market.

Memorandum circulars to implement Sections 2 and 3 of RA 8366 (Investment Houses Law) were issued liberalizing the Philippine Investment House Industry. These imposed a reciprocity requirement on foreign equity applications in investment houses, and specified the capital build-up requirements for investment houses from P200M to P300M.

Pending legislative initiatives to support administrative reforms have been deliberated in the last Congress but now need to be refiled with the present Congress. They include: the Revised Investment Company Act; Amended Corporation Code of the Philippines; and Pre-need Code.

To further enhance the development of capital market, efforts are geared towards the creation of a secondary bond market in the Philippines and the expansion of the small investor base. In line with this objective, the Department jointly with PSE launched a Joint Enforcement Program and established a Small and Medium Enterprises Board.

Insurance Commission

The Insurance Commission continued to pursue its task of regulating and supervising the insurance industry to ensure that adequate insurance protection is available to the public and to maintain the financial stability of the insurance industry. In 1998, the Commission issued a total of 27,506 licenses to insurance companies and its intermediaries, mutual benefit associations and trust for charitable uses. It approved 151 applications for investment instruments like Eurobonds, government bonds, stocks, guarantee loans and short-term investments. The Commission managed and administered the P10 million security fund of insurance companies and the Guaranty Fund set up by mutual benefit associations.

In furtherance of effective supervision and regulation of the insurance industry, the Commission maintains close cooperation with regional and international insurance supervisory authorities and other local and foreign government agencies. It hosted the 11th General Conference of the Association of Insurers and Reinsurers of Developing Countries on February 8-11, 1998.

Philippine Deposit Insurance Corporation

As of November 1998, the total insurance reserves of PDIC reached P18.4 billion or 20.4 percent higher than the P15.3 billion registered over the previous year. Premiums

collected increased by 24.2 percent, from P2.6 billion in 1997 to P3.3 billion in 1998.

Total deposit claims settled as of December 1998 amounted to P4.1 billion, representing 1.8 million accounts from 328 closed banks. For the year, 25,843 accounts worth P746.0 million were paid while the rest of the accounts were pending for lack of documentary requirements. Claims paid under the Emergency Pay-out Facility - claims needed immediate action for humanitarian reasons - amounted to P574 thousand.

A total of 40 banks were ordered closed by the Monetary Board during the year, of which 24 were taken over by the PDIC. As of end 1998, 316 banks were under PDIC liquidation management, with estimated realizable assets and liabilities of P10.6 billion and P11.2 billion, respectively.

The stress brought about by the currency crisis affected the banking industry. There were 23 closures registered in 1998. The PDIC extends assistance to distressed banks in consideration of a viable rehabilitation plan. Assistance may be in the form of placement of deposits, direct loans, purchase of assets, and assumption of liabilities. As of end 1998, there are only two banks under financial assistance with outstanding receivables aggregating P1.2 billion.

Central Board of Assessment Appeals

The Central Board of Assessment Appeals is a quasi-judicial, appellate collegial body that hears and decides elevated cases pertaining to real property tax assessment.

In 1998, the Board acted on 395 tax cases. Decisions made in most cases were favorable to the Government. The aggregate assessed value of the properties involved in these cases amounted to P3.4 billion.

Trade and Investment Development Corporation of the Philippines

The PHILGUARANTEE was renamed Trade and Investment Development Corporation (TIDCORP) on February 12, 1998 under its revised charter enacted through Republic Act 8494. This new law provides for the expansion of the Corporation's functions and its conversion into a full-pledged export credit agency. TIDCORP's outstanding guarantees as of December 31, 1998 amounted to P5.5 billion, reflecting an increase of 23 percent over the 1997 level of P4.5 billion. The recorded increase in outstanding guarantee was primarily attributed to the P1.1 billion increase in General Facility Program.

National Tax Research Center

The National Tax Research Center (NTRC), as the tax research arm of the DOF, continues to conduct research on taxation as basis for tax policy formulation and legislation consistent with the macroeconomic goals and objectives of the government. These include research studies on taxation, fiscal incentives, tax administration, and local government units. In 1998, the NTRC completed its major project entitled "Evaluation of the System of Implementation and Effectiveness of the Tax and Duty Privileges Granted to Economic Zone."

Among the other studies completed are the following: review of the internal revenue taxes imposed on automotive parts and accessories; review on the taxation of reverse repurchase papers; study on the viability of the socialized housing tax as a source of fund for local governments' infrastructure project; assessment of the tax on winnings under Section 126 and study on the expansion of the coverage of the excise tax on automobiles under Section 149 of the NIRC, respectively; review of the impact on individual income tax

provisions of the Comprehensive Tax Reform Package; five-year gradual phase-out of the gross receipts tax; re-examination of the documentary stamp taxes imposed on financial transactions; and reduction of the premium tax rate on life insurance premiums form 5 percent to 2 percent.

The NTRC extended technical and administrative assistance to the Task Force on Earmarked Revenues; the Task Force on Zonal Valuation; the Task Force on the Drafting of the Implementing Rules and Regulations of the Tax Reform Act of 1997 (R.A. No. 8424); Task Force on Revenues Waived; Task Force on the Revision of Fees and Charges; Task Force on the Financial Sector; Working Group of the Development Budget Coordinating Council / Executive Technical Board; and the Working Group on Reforming the Real Property Tax System through Process Innovation.

The NTRC also provided technical assistance to the local government units and handled the technical and secretariat function of the executive committee as well as the technical working groups on taxation, financial services, customs and local governments on the review of the Subic Bay Freeport Policy and Institutional Framework. As the Secretariat of the Fiscal Incentive Review Board (FIRB), it processed and evaluated applicants for tax subsidy availments requested by government-owned and controlled corporations for consideration of the FIRB Technical Committee and the Board Proper.

CHALLENGES AND DIRECTIONS

As the Philippine economy strives to recover from crisis, financing economic growth is an enormous challenge that faces the fiscal sector in general, and the DOF in particular. Likewise, pushing the remaining agenda of economic liberalization and deregulation will require significant effort in advocacy.

To respond to this challenge, the Department will have to implement the right mix of fiscal programs primarily through its tax administration, borrowing and privatization activities. Likewise, it will need to shepherd through Congress further economic restructuring bills to ensure their early passage.

Tax administration will be improved through further computerization of operations of BIR and BOC, plugging of loopholes and leakages in the revenue system and rationalization of fiscal incentives, among others.

Tax reforms will be implemented to remove remaining distortions in the tax system, enhance its equity features, and promote the protection of the environment. These include the rationalization of fiscal activities, the reform of the taxation of the financial sector, and the introduction of so-called "green" taxes.

As the economy becomes more integrated with the globalization of markets, electronic commerce is projected to become a significant mode of transactions worldwide in the years ahead. In this regard, the Department will have to brace itself with the issues on how products and transactions will be determined in the cyberworld.

The Department, through the Committee on Privatization (COP), will pursue more aggressive privatization program. A proof toward this direction is the issuance of Executive Order No. 12 on August 14, 1998 by President Estrada.

The EO widens the scope of privatization by including various government authorities such as the Bases Conversion and Development Authority (BCDA), Public Estates Authority (PEA), Philippine Tourism Authority (PTA), Philippine Economic Zone

Authority (PEZA) and the Subic Bay Metropolitan Authority (SBMA).

EO No. 12 also includes other modes of privatization such as leasing, management and maintenance contracts, build-operate-transfer (BOT) scheme and joint venture arrangements. These alternative modes are in addition to the traditional method of selling shares or assets, and they will be used to privatize infrastructure utilities like power, railways and airports.

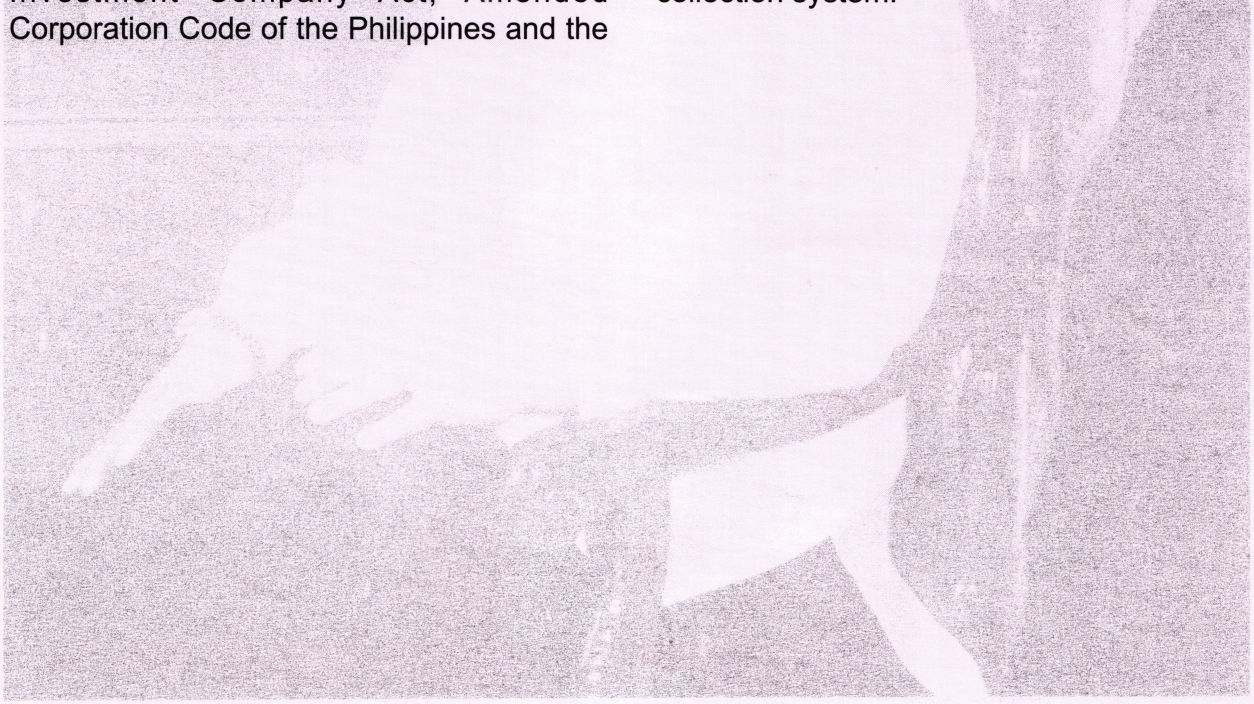
President Estrada has already asked the legislative branch to fast track the bill which allows for the privatization of the National Power Corporation and restructure the country's electricity supply industry. In 1999, the COP aims to privatize its remaining portfolio, with the power sector as a legislative priority.

The Department will push for the amendment of securities and investment-related laws to pave the way for greater investment participation. It is likewise pushing for the immediate enactment of the proposed Securities Act of 1998 and will vigorously pursue the immediate passage of the Revised Investment Company Act, Amended Corporation Code of the Philippines and the Pre-need Code.

The Department will continue to tap prudently and judiciously both domestic and foreign borrowings to finance shortfall of resources. Domestic borrowings will take into account the borrowing requirements of the private sector to avoid the "crowding out" effect and thus prevent an undue upward pressure on the domestic interest rates.

In the case of foreign borrowings, the Department will continue to focus on bilateral and multilateral funds since these provide lower interest rates and longer maturities but the government will continue to issue bonds for private sector investors.

The country's fiscal sector took a more proactive role as the Estrada Administration opted for an expansionary fiscal stance to stimulate the economy. Pump priming the economy remains the focus of fiscal policy over the next two years. Attaining a balanced budget and reverting to fiscal surpluses in the medium-term pose a big challenge to the Department. This early, the Department faces the difficult task of building the foundation of buoyant, efficient and effective revenue collection system.



The Secretary of Finance

HON. EDGARDO B. ESPIRITU

The Undersecretaries

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(DFG)

Solomon S. Cua
Revenue Operations Group
(ROG)

Joel A. Bañares
Corporate Affairs Group (CAG)
International Finance Group (IFG)

Lily K. Gruba
Policy Development &
Management Services Group
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Ma. Eleanor F. dela Cruz
Policy Development &
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Gil S. Beltran
Domestic Finance Group (DFG)

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Thelma A. Mariano
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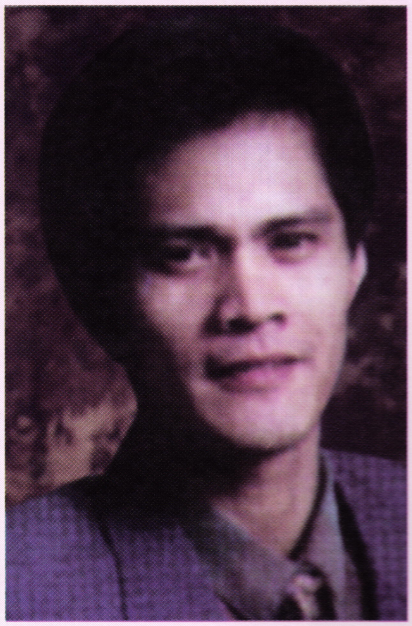
The Directors

Concepcion S. Kimpo
Director IV
Revenue Office



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Jeremias N. Paul, Jr.
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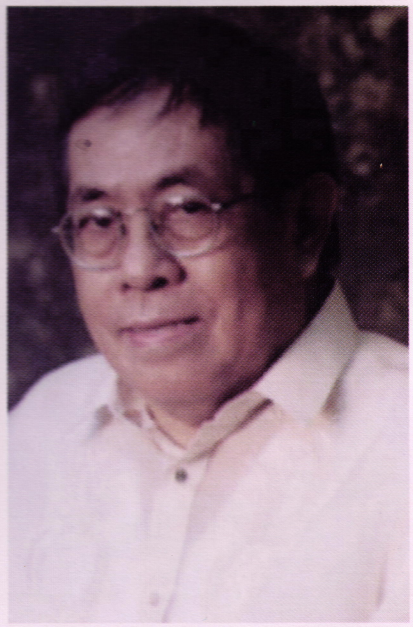

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Vicente G. Quintos
Executive Director
National Tax Research Center

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President
Trade and Investment Development Corporation of the Philippines

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Undersecretary	**Undersecretary**	**Undersecretary**	**Undersecretary**

GIL S. BELTRAN	MA. ELEANOR F. DELA CRUZ
Assistant Secretary	**Assistant Secretary**

Domestic Finance Group	Policy Development & Management Services Group	Corporate Affairs Group	International Finance Group	Revenue Operations Group
FISCAL POLICY AND PLANNING OFFICE	CENTRAL FINANCIAL MANAGEMENT OFFICE	CORPORATE OPERATIONS OFFICE	INTERNATIONAL FINANCE POLICY OFFICE	REVENUE OFFICE MABUHAY-LANE
	CENTRAL ADMINISTRATION OFFICE	PRIVATIZATION OFFICE	INTERNATIONAL FINANCE OPERATIONS OFFICE	LEGAL AFFAIRS OFFICE
	INFORMATION AND LIAISON OFFICE			ONE-STOP SHOP TAX CREDIT AND DUTY DRAWBACK CENTER

BIR	BOC	BTr	BLGF	EIIB	SEC	IC	NTRC	FIRB	CBAA	PDIC	TIDCORP

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DEPARTMENT OF FINANCE
1998 Annual Report

Produced by:
HYPERPRINT CORPORATION

Designed by:
SCITECH OUTDOOR ADVERTISING, INC.

DEPARTMENT OF FINANCE
Roxas Boulevard cor. P. Ocampo St.
Manila