



OECD Competitive Neutrality Reviews

PHILIPPINES

SMALL-PACKAGE DELIVERY SERVICES



OECD Competitive Neutrality Reviews: Small-Package Delivery Services in the Philippines

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Foreword

Southeast Asia, one of the fastest growing regions in the world, has benefited from a broad embrace of economic growth models based on international trade, foreign investment and integration into regional and global value chains. Maintaining this momentum, however, will require certain reforms to strengthen the region's economic and social sustainability. This will include reducing regulatory barriers to competition and market entry to help foster innovation, efficiency and productivity.

The logistics sector plays a significant role in fostering economic development. Apart from its contribution to a country's GDP, a well-developed logistics network has an impact on most economic activities. An efficient logistics system can improve a country's competitiveness, facilitate international trade and enhance its connectivity to better serve consumers and meet the needs of regionally integrated production facilities for reliable delivery of inputs and outputs.

The *OECD Competitive Neutrality Reviews: Small-Package Delivery Services in the Philippines*, undertaken within the framework of the ASEAN Competition Action Plan, assesses the impact of state-owned enterprises on competition in the Philippines. The analysis focuses on small-package delivery services, a fundamental part of the logistics sector due to their important role in the rapidly growing e-commerce sector. In parallel, the OECD has assessed the impact of regulation on competition in the logistics sector in the *OECD Competition Assessment Reviews: Logistics Sector in the Philippines*.

The OECD assessment was conducted in consultation with the Philippine authorities and with local stakeholders, with the support of the ASEAN Secretariat and the UK Prosperity Fund (UK Government). The assessment prioritises 56 pieces of legislation and identifies 23 regulatory barriers where changes could be made to foster competition in the small-package delivery services by levelling the playing field between public and private companies. This could benefit the Philippines significantly as in the recent past e-commerce has grown less rapidly than other countries in Asia, but this trend seems to be changing. This report offers policy recommendations that can help the Philippine government address structural and regulatory shortcomings in the small package delivery services sector.

These structural reforms have become even more pressing as the Philippine economy is expected to contract by 7.3% in 2020 (compared to a growth rate of 6% in 2019) due to the COVID-19 pandemic, with containment measures severely affecting key economic activities such as exports and tourism. These policy recommendations contribute to reforms that can help the Philippine economy resume sustainable growth and job creation, by enhancing competitiveness, encouraging investment and stimulating productivity in the logistics service sector, with knock-on economy-wide effects and benefits for its consumers.

I congratulate the Philippine government, as well as the ASEAN Secretariat and the UK Prosperity Fund (UK Government), on their efforts to lift regulatory barriers to competition and to improve the business environment. The OECD looks forward to continuing and broadening its co-operation with ASEAN to support further its reforms to the benefit of its citizens.

Greg Medcraft



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- Philippine Postal Corporation (PHLPOST)
- the Governance Commission for Government-Owned or Controlled Corporations (GCG)
- the Postal Regulation Division
- Department of Information and Communications Technology
- the Land Transportation Office (LTO)
- Department of Transportation; the Privatization and Management Office (PMO)
- Department of Finance; and the Department of Trade and Industry

The following trade associations and private companies were interviewed:

- the Confederation of Truckers Association of the Philippines (CTAP)
- LBC Express
- the Supply Chain Management Association of the Philippines (SCMAP)

The ASEAN Secretariat and Ms Lai-Lynn Angelica B. Barcenas, partner at Barcenas Barcenas & Partners Law Offices, provided valuable inputs.

The OECD project team consisted of Ruben Maximiano, Senior Competition Expert and ASEAN Project Co-ordinator; Wouter Meester, Competition Expert and Competitive Neutrality Project Leader; Matteo Giangaspero, Competition Expert; Michael Saller, Senior Competition Expert and Competition Assessment Project Leader; Sophie Flaherty, Competition Analyst; and Gaetano Lapenta, Competition Analyst, all from the OECD Competition Division. The report was drafted by Matteo Giangaspero and Wouter Meester, edited by Tom Ridgway and prepared for publication by Eleonore Morena and Erica Agostinho.

Valuable comments throughout the process and on the final report were provided by Antonio Capobianco, Acting Head of the OECD Competition Division, and Hans Christiansen, Senior Economist; Sara Sultan, Policy Analyst; and Chung-a Park, Policy Analyst, all three of the OECD Corporate Affairs Division. Leni Papa, first as independent consultant to the OECD and later as part of the OECD Competition Division, also provided significant input to the report.

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The information and figures in the report are updated as of October 2019, while economic forecasts have been updated with more recent figures reflecting the impact of the COVID-19 pandemic.

The findings in this report are the result of an independent assessment by the OECD based on an analysis of selected (prioritised) Philippine legislation, stakeholder interviews and desk research.

Fostering competition in ASEAN

ASEAN Member States have agreed to implement significant reforms towards market liberalisation and elimination of competition distortions as part of the ASEAN Competition Action Plan 2016-2025 (ACAP 2016-2025) which provides strategic goals, initiatives and outcomes to fulfil the competition-related vision of the AEC Blueprint 2025. In order to increase awareness of the benefits and role of competition in ASEAN, the ACAP 2016-2025 provides for an assessment to be conducted on the impact of non-tariff barriers on competition in the markets of ASEAN Member States followed by recommendations.

The logistics sector was chosen by the ASEAN Secretariat and ASEAN Expert Group on Competition (AEGC) as it can play a significant role in increasing ASEAN's economic development, and is included in the AEC Blueprint's 12 priority integration sectors. Indeed, efficient logistics can play a significant role in increasing a country's economic development by facilitating international trade and improving its competitiveness. By developing an efficient logistics system, a country can enhance its connectivity to better serve its importers and exporters, and satisfy the needs of regionally integrated production facilities for reliable just-in-time delivery of inputs and outputs.

Against this background, the ASEAN Secretariat, with funding from the UK Prosperity Fund (UK Government), tasked the OECD to assist with the implementation of Initiatives 4.1 and 4.2 of the ACAP 2016-2025. These two initiatives require an assessment of the impact of competition law and policy on the markets of all 10 ASEAN Member States, both in general (4.1) and with a focus on state-owned enterprises (4.2).

This report contributes to ACAP Outcome 4.2.1 (Impact of state-owned enterprises and government-linked monopolies on competition), building on a competitive neutrality assessment in the small-package delivery services sector.

The current report on the Philippines is part of a series of 10 similar assessments (one for each ASEAN Member State).

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Acronyms and abbreviations

3PL	Third-party logistics
ACAP	ASEAN Competition Action Plan
AEC	ASEAN Economic Community
AEGC	ASEAN Experts Group on Competition
APEC	Asia-Pacific Economic Cooperation
ASC	Authorised service contractor
ASEAN	Association of Southeast Asian Nations
B2B	Business-to-business commerce
B2C	Business-to-consumer commerce
BOC	Bureau of Customs
CEO	Chief executive officer
CGS	Corporate governance scorecard
COA	Commission on Audit of the Philippines
CPCS	Compensation and position classification system
CSO	Corporate Standards Office
DBM	Department of Budget and Management
DICT	Department of Information and Communications Technology
DICT-PRD	Postal Regulation Division of DICT
DOLF	Directors' and Officers' Liability Fund
DOLI	Directors' and Officers' Liability Insurance
EABC	European Association for Business and Commerce
GCG	Governance Commission for Government-Owned and Controlled Corporations
GLC	Government-linked company
GLM	Government-linked monopoly
GSIS	Government Service Insurance System
ICT	Information and communications technology
MC	Memoranda Circulars
MO	Memoranda Orders
NEDA	National Economic and Development Authority
OSP	Outside service providers
PCC	Philippine Competition Commission
PMO	Privatization and Management Office
PSO	Public-service obligation
PUD	Pick-up and delivery
SEC	Securities and Exchange Commission
SOE	State-owned enterprise
SPDS	Small-package delivery services
UPU	Universal Postal Union

Executive summary

State-owned enterprises and competition

Assessing the impact of state-owned enterprises (SOEs) on competition is important because competitive neutrality – state-owned and private businesses competing on a level playing field – ensures that all enterprises, public or private, domestic or foreign, face the same sets of rules. In order to ensure optimal economic outcomes, SOEs should compete against private entities on fair terms, while recognising and taking into account their contribution to socio-economic and policy objectives.

SOEs may enjoy rights or privileges unavailable to private competitors, which give them undue competitive advantage over their rivals, including selective subsidies, explicit or implicit loan guarantees, preferential purchasing, preferential standards, support for unnecessary new capacity, and regulatory or tax favouritism. This may make market entry more difficult for private companies (both domestic and foreign) and can therefore also constitute a competitive obstacle. However, SOEs may be subject to certain duties, such as a requirement to operate (underfinanced) public services or the need to comply with civil-service labour rules, which affect their ability to compete effectively with privately owned competitors.

A level playing field between public and private market participants leads to more choice, higher quality and lower prices for consumers and ultimately benefits economic growth and development. For example, research has shown that financially disadvantaged consumers often suffer disproportionately from the exercise of market power. A level playing field also benefits taxpayers as (often limited) public resources can be better allocated to other public services, including pensions, healthcare and social benefits. Finally, research has shown that including gender considerations in competition policy can improve gender equality.

PHLPOST and the small-package delivery services sector in the Philippines

The Philippines, an archipelago comprising about 7 641 islands, is classified by the World Bank as a lower-middle income country. It had a gross domestic product (GDP) per capita of USD 3 103 in 2018, which made it the sixth country in ASEAN (in terms of per capita GDP). Its economy grew approximately 6.5% a year between 2013 and 2018, which enabled it to outpace average growth in ASEAN in the same period. The Philippines has been a member of ASEAN since the association's founding in 1967.

SOEs, or government-owned or controlled corporations (GOCCs) as they are known in the Philippines, play an important role in the country. Nationalisations in the mid-1960s, together with the declaration of martial law in 1972, boosted the presence and prominence of the GOCC sector, leading to over 600 GOCCs by 2010.

Philippine Postal Corporation (PHLPOST) is wholly owned by the state and is the designated postal operator for the Philippines' Universal Postal Union (UPU) obligations. As such, PHLPOST is responsible for the delivery of mail and parcels "throughout the Philippines", as well as the development and operation of a network that "extends or makes available, at least ordinary mail service, to any settlement in the country".

A level playing field in the small-package delivery services (SPDS) sector is crucial for developing a competitive market and fulfilling the sector's potential so as to reap full benefits from international developments. The Philippine SPDS sector is regulated by a substantial body of legislation, with the main piece being the Postal Service Act, which established PHLPOST in 1992.

Preventing the existence of a level playing field in the Philippine SPDS sector are several obstacles that may harm competition, hinder the Philippine economy, and stop consumers from fully benefiting from a rapidly developing e-commerce market; a trend that is further increased and accelerated by the covid-19 pandemic.

Some of these obstacles are linked to or affected by PHLPOST's joint role: it has both a legal monopoly in the letters and postcards segment *and* competes with privately owned businesses in the highly competitive SPDS market. As has also been observed in many countries around the world, electronic communications are leading to drastic falls in the volume of traditional letters and postcards in the Philippines, increasing the commercial importance of the SPDS market to the incumbent postal operator, PHLPOST.

This situation is similar to that of many OECD countries in the late 1990s, when postal services were provided by monopoly operators and technological developments began to erode incumbent postal operators' core businesses, potentially threatening their ability to continue financing their social obligations such as universal service. These monopoly operators were mostly state-owned, protected from competition, and enjoyed certain benefits over their privately owned competitors.

Since the 1990s, many OECD countries have addressed the issue of levelling the playing field between incumbent postal operators and private competitors also active in (contestable) commercial markets. In these countries, the SPDS sector was gradually opened up to competition, leaving the postal sector either entirely or partly to the incumbent postal operator.

While there are different options to improve the level playing field in the SPDS sector, such as regulation and deregulation, liberalisation and privatisation, PHLPOST's rights, privileges and duties (or advantages and disadvantages) are often interrelated and should therefore be looked at as a whole. Addressing the obstacles to competition in the SPDS sector in the Philippines requires a holistic approach. For instance, any actions that aim to reverse or decrease PHLPOST's rights and privileges should be accompanied by a clear assessment of the impact and possible disadvantages that result from PHLPOST's public-service obligation (PSO), including the compensation mechanism. In other words, any measures to improve the competitiveness of the SPDS sector must take into account that PHLPOST's viability can only be assured when it is adequately compensated for the fulfilment of its PSO.

Key recommendations

This report identifies 23 recommendations that aim to improve the level playing field in the Philippine SPDS sector. If fully implemented, these recommendations can be expected to generate significant benefits to the Philippine economy, and more broadly to ASEAN. Full implementation of the recommendations set out in this report can be expected to deliver positive long-term effects on employment, productivity, growth and improve the ability of businesses to compete.

It is important to note that the number of recommendations in this report is neither indicative of the overall restrictiveness of logistics regulation in the country, nor a good basis for comparisons between countries. Firstly, some restrictions to competition identified by the OECD are more harmful than others, making comparison between countries difficult and often not very meaningful. Secondly, the number of recommendations depends on several factors including the number of pieces of legislation available and reviewed as well as the amount and depth of contributions and feedback from domestic stakeholders.

The main recommendations are:

- Adequately compensate PHLPOST for the fulfilment of its PSO; based on other countries' experience, the PSO can be funded in various forms including: a) direct or indirect transfer payments from the government; b) granting access to PSO through public procurement; or c) contributions of other service providers or their users into a universal PSO fund.

- Adequately compensate franking privilege services; this can take various forms (such as foregone dividends by the state), as long as they are identified and properly accounted. Compensation should be detailed in legal provisions or through contractual mechanisms, rather than ex post negotiations. The contractual mechanism should take into account, for instance, the quality of franking privilege services using objective criteria. Moreover, compensation may be periodically adjusted taking into account any quality improvements in PHLPOST's franking privilege services.
- Ensure that PHLPOST keeps separate accounts for the provision of franking privilege services.
- Limit the cases where PHLPOST's ownership entity needs to obtain the Philippine president's ex ante approval for significant transactions, such as high-risk transactions or transactions exceeding a certain value.
- Subject PHLPOST's financial statements to independent external audit.
- Amend the Postal Service Act to clarify that PHLPOST does not exercise any regulatory powers on the industry.
- Ensure that the DICT Act and the Implementing Rules and Regulations of the DICT Act explicitly state that Department of Information and Communications Technology (DICT) executes the regulatory role in the relevant sector.
- Ensure that the DICT Act and the Implementing Rules and Regulations of the DICT Act explicitly state that Postal Regulation Division of DICT (DICT-PRD) regulation applies equally to PHLPOST and its SPDS competitors.
- Amend Section 12 of the Postal Service Act to reflect that the state will not grant any preferential (financial) treatment to PHLPOST.
- Consider mechanisms (such as guarantee fees) that impose compensatory payments to the Bureau of the Treasury from GOCCs that benefit from lower borrowing costs thanks to state guarantees, compared to private companies in comparable circumstances.
- Ensure that PHLPOST's relations with state-owned financial institutions are on commercial terms and minimise the risk of conflicts of interests, such as PHLPOST's directors also sitting on the boards of state-owned banks.

1 Introduction

1.1. Scope of the report

State-owned enterprises (SOEs) play a significant role in the Philippines as in many other national economies around the world. In order to ensure optimal economic outcomes, SOEs should compete with private entities on a level playing field, while recognising their contribution to socio-economic and policy objectives.

This report assesses the impact of state-owned enterprises on competition in the Philippines, identifying the key advantages or disadvantages of state-owned enterprises when competing with private companies. The analysis focuses on the logistics sector, and more specifically on small-package delivery services. Efficient logistics can play a significant role in increasing a country's economic development by facilitating international trade and improving its competitiveness. Small-package delivery services are a fundamental part of the logistics sector due to their important role in the rapidly growing e-commerce sector.

1.2. The impact of COVID-19 on e-commerce

The COVID-19 pandemic is disrupting global supply chains in unprecedented ways and will have a significant economic impact with GDP contractions in most ASEAN member states in 2020. As in other countries, due to COVID-19 and the resulting restrictions to contain the pandemic, ASEAN member states are facing a decline in consumption, investment, and trade, with a severe impact on key sectors such as tourism. Nevertheless, COVID-19 should not affect the long-term progress of ASEAN, driven by its middle-class boom. In September 2020, the Asian Development Bank (ADB) revised its estimates for GDP growth in Asia in 2020 and 2021. According to the ADB (ADB, 2020^[1]), Southeast Asia's (i.e. ASEAN member states + Timor-Leste) GDP is expected to contract 3.8% in 2020 and rebound to 5.5% in 2021. For the Philippines, the ADB expects that the economy will contract by 7.3% in 2020 because of the COVID-19 epidemic but that recovery is expected in 2021. In 2019, the recorded GDP growth rate was 6%, while the 2021 GDP growth forecast is 6.5%.

The pandemic has provoked an abrupt and sharp increase in the use of e-commerce. For instance, in the week of 22 March 2020, weekly downloads for shopping applications in Thailand are estimated to have increased by 60%, while Indonesia, Singapore and Viet Nam each recorded a 10% increase (OECD, 2020, p. 99^[2]). E-commerce is likely to keep growing as consumers continue to shun physical stores in favour of online shopping solutions (ASEAN, 2020^[3]).

The COVID-19 crisis will lead to long-term changes. It is likely to expedite the shift to e-commerce, especially for consumers that were until recently more resistant to online retail channels. Brick-and-mortar businesses will also evolve offering services beyond retail, including last-mile deliveries. Digital transformation is occurring rapidly in ASEAN. For instance, Cambodia, Lao PDR and Myanmar recorded an annual growth of approximately 20% in e-commerce users in April 2020 compared to the previous year. In terms of value of online sales, high annual growth rates (above 15%) were recorded in Indonesia, Thailand, the Philippines and Malaysia. Moreover, COVID-19 is expected to accelerate governments' and businesses' initiatives to provide connectivity to "vulnerable communities", removing barriers for SMEs, and providing easier access to products with better price and quality (World Economic Forum, 2020^[4]).

Notwithstanding the above, e-commerce deliveries often remain expensive and unreliable because of barriers to logistics services, at least in some ASEAN member states. This affects the development of e-commerce, both domestically and internationally. Lifting such barriers would support the development of e-commerce and provide consumers with more choice and better prices.

Regional co-operation plays and will continue to play a key role in this context. ASEAN has put in place a framework for COVID-19 responses across multiple sectors (United Nations, 2020^[5]). Moreover, the ASEAN Expert Group on Competition (AEGC) released a joint statement in Response to the COVID-19 Pandemic.¹ APEC is also taking collective initiatives. In May 2020, the ministers responsible for trade in APEC economies pledged to work together to mitigate the impact of COVID-19, committing (among other considerations) to facilitate the flow of goods across borders, as well as to strengthen e-commerce and related services (OECD, 2020, p. 99^[2]).

1.3. Report structure

The report is structured as five chapters. This executive summary outlines the content of the report and provides an overview of its key recommendations; Chapter 1 defines state-owned enterprises and the relationship between state-owned enterprises and competition policy; Chapter 2 provides an overview of the economic importance and the legal framework of state-owned enterprises in the Philippines; Chapter 3 describes the competitive landscape and the regulation applicable to small package delivery services in the Philippines; Chapter 4 focuses on PHLPOST, the state-owned enterprise providing SPDS in the Philippines and the advantages or disadvantages that can impact on competition, and offers recommendations to improve the level playing field.

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Note

¹ See <https://asean.org/asean-experts-group-competition-releases-statement-response-covid-19>

2 State-owned enterprises and competition

2.1. Introduction

SOEs play a significant role in many national economies around the world. Approximately 22% of the world's largest 100 firms are estimated to be effectively under state control, with many of these operating key upstream and downstream activities in international supply chains, such as public utilities, manufacturing, metals and mining, and petroleum (OECD, 2016^[1]).

The role and importance of SOEs differ substantially between regions, countries and sectors. In Southeast Asia, they still represent a major part of many economies, measured by percentage of GDP, employment and fiscal revenues, and remain indispensable players in almost all key sectors, building, maintaining and operating critical infrastructure, delivering critical services, and providing public employment. Their characteristics as publicly owned enterprises allow them to play a critical role in most economies and to contribute to developmental goals that – in practice – often result from other (political or economic) objectives (OECD, 2015^[2]).

In order to ensure optimal economic outcomes, however, SOEs should compete against private entities on level playing fields that nevertheless recognise – to an appropriate and relevant extent – their socio-economic and developmental roles and policy objectives.

Several member states of ASEAN have begun considering SOE reform in view of improving economic outcomes; this has seen differing results. These states could capitalise on the experiences of different OECD countries, including those cited in the *OECD Guidelines on Corporate Governance of State-Owned Enterprises* (OECD, 2015^[3]).¹ In OECD countries (and beyond), SOEs' roles evolved significantly between 1990 and 2010, with large privatisation initiatives throughout the 1990s and early 2000s (OECD, 2018^[4]; 2009^[5]; 2019^[6]). At the same time, many governments have sought to rationalise the enterprises they continue to own, subjecting them to the same laws and treatment as private enterprises and professionalising their ownership and governance.

2.2. Definition of SOEs

An SOE is an enterprise entirely or partly owned by the state; it can be organised in different forms and serve a wide range of functions. Certain countries, including ASEAN member states, use different terms including state-owned companies, state-owned entities, state enterprises, publicly owned corporations, government-linked monopolies (GLMs), or government-linked companies (GLCs).

The OECD's definition of an SOE, as defined in the *OECD Guidelines on Corporate Governance of SOEs*, recognises such diversity and focuses on entities' corporate forms, commercial orientation, and degree of state ownership and control:

“any corporate entity recognised by national law as an enterprise, and in which the state exercises ownership, should be considered as an SOE. This includes joint stock companies, limited liability companies and partnerships limited by shares. Moreover statutory corporations, with their legal personality established through specific legislation, should be considered as SOEs if their purpose and activities, or parts of their activities, are of a largely economic nature.” (OECD, 2015, pp. 14-15^[3])

For the purpose of this report, the following factors are relevant in determining whether an entity is an SOE, and more broadly, in terms of competition policy.

1. Ownership structure

- a. **Enterprise wholly owned by the state.** An enterprise under a nation’s laws over which the state exercises full ownership is more than likely to be an SOE. An enterprise’s institutional form, such as a company limited by shares or partnership, is not generally determinative.
 - b. **Enterprise controlled by the state.** An enterprise controlled by the state should ordinarily be considered an SOE. “Control” should be assessed in a substantive way, and may require case-by-case assessment. It would normally be established in cases where the state, by directly or indirectly holding a majority of the voting rights in an enterprise, exercises influence over an enterprise’s strategic decisions, such as approval of budgets, business plans and major investments, as well as the appointment of senior management.² In countries where the state invests in a wide range of companies through sovereign wealth funds or publicly owned holding companies, the state’s control may be indirectly exercised; this may require an assessment. The state can exercise an equivalent degree of control in situations where, for example, an enterprise’s by-laws allow the state to appoint the majority of the board of directors or assign a “golden share” that gives veto rights for certain strategic decisions. Not all ownership amounts to control, however. For instance, small equity holdings of less than 10% held by independent asset managers such as public pension funds would not ordinarily amount to control and an enterprise would not be considered an SOE. Similarly, enterprises temporarily controlled by the state in the course of bankruptcy or similar procedures would not ordinarily be SOEs.
- 2. Economic nature of activities.** An entity established by law whose purposes or activities are largely economic in nature would be considered an SOE. An economic activity is one that involves offering goods or services in a given market and which could, at least in principle, be carried out by a profit-seeking private operator. Economic activities mostly take place in markets open to competition or where competition could occur, given existent laws and regulations.

2.3. Benefits of competition

There is broad consensus that competition creates significant benefits for consumers. When consumers can choose between different providers of goods or services, firms are forced to compete with each other, innovate more, and be more productive. Consumers benefit from more choice, advanced products and services, higher quality and lower prices. Competition ultimately enhances productivity growth and consumer welfare.

On a macroeconomic level, this productivity growth leads to faster growth for the overall economy. Empirical evidence demonstrates that improving market regulation to make competition work increases productivity in affected markets and ultimately stimulates faster economic growth and job creation. Where binding and significant regulatory restrictions on competition are eliminated, prices may fall by as much as 20% (OECD, 2014^[7]). For instance, when Australia engaged in broad pro-competitive regulatory reforms in the 1990s, its Productivity Commission estimated that these reforms resulted in a GDP increase of at least 2.5%. Importantly, research has shown that competitive restrictions have a disproportionately negative impact on the poor meaning that pro-competition policies, by eliminating cartel-like market

conditions, can substantially enhance living standards for the economically disadvantaged or impoverished by reducing prices and increasing real income (Ennis, Gonzaga and Pike, 2017^[8]).

Given these benefits, competition can also play an important role in achieving other government policies, including those promoting consumer protection, entrepreneurship, innovation, investment, corporate governance, equal opportunities, effective public procurement, open trade, growth and competitiveness. Competition benefits are also the reason for governments' liberalisation and deregulation policies, notably in network industries.

That said, sound and effective competition does not always arise naturally: the temptation is strong for economic players to restrict competition to achieve greater profits.

2.4. SOEs and competitive neutrality

SOEs' anti-competitive behaviour can be as harmful as restrictions of competition by private competitors. Governments and competition authorities must recognise the fundamental role of competition law and policy in markets where publicly and privately owned entities are (or could be) competing with each other.

At ASEAN level, the *Economic Community Blueprint 2025* affirms that one of the elements necessary to increase the region's productivity is to ensure "a level playing for all firms, regardless of ownership". This is also identified as the fundamental goal of competition policy and law.³ These principles are also noted in the 2010 *ASEAN Regional Guidelines on Competition Policy*, in which the ASEAN Expert Group on Competition (AEGC) stated that: "Competition policy should be an instrument of general application, i.e., applying to all economic sectors and to all businesses engaged in commercial economic activities (production and supply of goods and services), including State-owned enterprises" (ASEAN, 2010^[9]). This results in no ASEAN competition law giving SOEs a general exemption.

The ultimate objective is to level the playing field between privately owned entities and entities owned by, or linked to, the state, so that no business entity has advantages or disadvantages that result solely from its ownership (OECD, n.d., pp. 62-63^[10]). This principle, broadly known as competitive neutrality, should address distortions of competition caused by the state playing an active role in commercial markets.

The rationale for pursuing competitive neutrality is both economic and political. The main economic rationale is that it enhances allocative efficiency throughout the economy. Where certain agents – whether state-owned or private – are put at an undue disadvantage, goods and services are no longer produced by those who can do it most efficiently. This leads to lower real income and suboptimal use of scarce resources relative to a baseline scenario, such as inefficient production methods or the non-adoption of new and better technologies (OECD, n.d., p. 39^[11]).

The political rationale is linked to governments' roles as universal regulators in ensuring that economic actors are on a level playing field (in terms of state-owned corporate assets and other market participants), while also ensuring that PSOs are being met. Although the political commitment to maintaining a level playing field is generally strong, state-led commercial activities may still damage the competition landscape due to deliberate or unintentional departures from neutral practices (OECD, 2012^[12]).

2.4.1. SOEs and departures from competitive neutrality

Governments may take deliberate decisions to depart from competitive neutrality in cases where SOEs may be necessary to correct market failures or to achieve other policy objectives. In other words, governments' choices for non-neutrality include both economic rationales (circumstances where the economic outcome may be made more efficient through intervention), and broader policy rationales (in which case social objectives may justify exceptions to economic efficiency principles) (OECD, 2012^[12]; Capobianco and Christiansen, 2011^[13]).

A common economic rationale is the correction of market failures in specific markets. While the majority of markets may be best served by suppliers pursuing ordinary commercial objectives, certain markets have special characteristics that can lead to “market failures”, in which the ordinary interaction of supply and demand does *not* lead to the most economically efficient outcome. In such identifiable circumstances, an SOE whose operating principles depart from ordinary profit maximisation may achieve the most efficient attainable outcome.

The rationale for correcting market failures is most widely seen in industries with “natural monopoly” characteristics where – due to cost structures – it would not be economically efficient or likely in practice for competitors to operate. This effect is particularly common in network industries and utility industries, such as segments of the telecommunications and electricity industries, and domestic water supply, where economies of scale and network effects often legitimise the presence of a single provider.

A further economic rationale is that in some markets, “externalities” – wider social benefits or costs not captured in the price – associated with a product or service may make the market outcome inefficient, justifying provision of the product or service through an SOE.⁴

Beyond these economic rationales for SOEs, a number of broader policy rationales may also be relevant. First, governments may identify certain basic services that should be accessible to all members of society through a provider with a PSO. Such services typically include: 1) communication services such as postal services and telecommunications; 2) utilities such as electricity and water distribution; and 3) basic education. A PSO requires the provision of a minimum service to all consumers, often including those in sparsely populated areas where provision is uneconomic; it does not necessarily require the presence of an SOE and instead may be imposed on privately owned operators, with loss-making services compensated through cross-subsidisation from other services or direct government transfers (or both). Governments may decide, however, that it is more effective to achieve the social objective through an SOE rather than a privately owned operator.

Furthermore, governments may have strategic or industrial policy objectives in exercising ownership rights over certain industries. These national interest objectives may include:

1. protecting the viability of sectors that are viewed as being of systemic importance
2. maintaining state ownership of strategic industries (for instance, national defence)
3. supporting nascent or emerging industries that may be seen as strategically important in the future
4. more broadly, achieving developmental goals.

In addition, governments may have fiscal objectives for SOEs, such as ensuring a profit stream from the SOE to the national budget.

Finally, other political objectives may include the support of interest groups, such as public employees. For instance, SOEs remain a major source of employment and can provide better conditions than those in the private sector (OECD, 2017_[14]).⁵

When analysing the level playing field between public and private entities, the socio-economic and developmental role and policy objective of an SOE should be considered. A key aspect is to have full transparency around these objectives.

2.4.2. Key distortions of competition by SOEs

Whether intentional or not, departures from competitive neutrality can result in significant distortions of competition. An SOE’s market competitiveness can be enhanced (or impaired) through government ownership or connections in a number of ways.⁶

1. Financial treatment

- a. **Outright subsidies.** SOEs may receive direct state subsidies – not equally accessible to others – or may benefit from other forms of public financial assistance to sustain their commercial operations, such as favourable tax regimes or exemptions, or in-kind benefits.
- b. **Concessionary financing and guarantees.** SOEs may enjoy credit provided directly by governments or through state-controlled financial institutions at below-market interest rates. Explicit or implicit state guarantees are also linked to this distortion.

2. Asymmetrical regulation

- a. **Monopolies and advantages as incumbents.** Governments may entrust SOEs with exclusive or monopoly rights over some activities. This may foreclose access to competitors, and enhance SOEs' competitiveness in other markets open to competition, for instance, through cross subsidisation.
- b. **Other preferential treatment by the government.** SOEs may not be subject to the same, often costly regulatory regimes as private firms. Examples include exemptions from compliance with disclosure requirements and antitrust enforcement or preference in accessing public procurement.

3. Corporate governance

- a. **Lack of structural separation.** SOEs may be entrusted with both commercial and regulatory functions.
- b. **Captive equity.** SOEs' equity is generally "locked in", meaning control of an SOE cannot be transferred as easily as in privately owned firms. The absence of any risk of takeover and exemptions from bankruptcy rules can result in distortions in SOE managements' incentives to operate efficiently.

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Notes

¹ In this context, the OECD-Asia Network on Corporate Governance of State-Owned Enterprises provides a forum for the governments of Asian countries and corporate governance practitioners to share good practices and identify common priorities for strengthening SOEC corporate governance.

² EU Commission Consolidated Jurisdictional Notice under Council Regulation (EC) No. 139/2004 on the control of concentrations between undertakings ("Merger Regulation"), [https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:52008XC0416\(08\)](https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:52008XC0416(08)), paragraphs 65-73.

³ *AEC Blueprint 2025*, paragraphs 25-26. See also *AEC 2025 Consolidated Strategic Action Plan*.

⁴ The provision of education is a broadly accepted example of a service that has a positive externality beyond the immediate recipient. Basic research is also commonly mentioned as potentially being the subject of market failures leading to under-provision.

⁵ This number focuses on full- and majority-owned enterprises. When the analysis is expanded to include minority-owned listed companies, employment share rises considerably in some countries. Moreover, this number is likely to be much higher outside the OECD area.

⁶ For a more elaborate description, see Capobianco and Christiansen (2011_[13]).

3 SOE framework and the importance of SOEs in the Philippines

3.1. Introduction

The Philippines is an archipelago made up of 7 641 islands, with a population in 2017 of almost 105 million people.¹ It is a constitutional republic with a presidential system; the president of the republic assumes the role of both head of state and head of the government.

The Philippines is classified by the World Bank as a lower-middle income country. In 2018, its gross domestic product (GDP) per capita was USD 3 103, which made it the sixth country in ASEAN (in terms of per capita GDP). Its economy grew approximately 6.5% a year between 2013 and 2018, outpacing average growth in other ASEAN countries (approximately 5% a year between 2013 and 2017).² The Philippines recorded a GDP growth of 6% in 2019. Due to COVID-19, its GDP is now expected to contract 3.8% in 2020 and rebound to 6.5% in 2021. The Philippines ranked 64th in the World Economic Forum's 2019 Global Competitiveness Index 4.0, falling eight places compared to the 2018 Index (World Economic Forum, 2019_[1]). The Philippines is a signatory to ASEAN, APEC, the World Trade Organization, and the East Asian Community trade bloc.

3.2. The scope and importance of SOEs in the Philippines

In the Philippines, SOEs are referred to as government-owned or controlled corporations (GOCCs). A minimum government ownership, defined as 50%+1 of the outstanding capital, qualifies entities as GOCCs.

In particular, GOCCs are defined as “any agency organised as a stock or nonstock corporation, vested with functions relating to public needs whether governmental or proprietary in nature, and owned by the Government of the Republic of the Philippines directly or through its instrumentalities either wholly or, where applicable as in the case of stock corporations, to the extent of at least a majority of its outstanding capital stock”.³

There are two main categories of GOCCs in the Philippines:⁴

1. **Non-chartered GOCCs.** Non-chartered GOCCs are organised under the Corporation Code of the Philippines (Batas Pambansa Bilang 68)⁵ and are subject to civil-service rules.⁶
2. **Chartered GOCCs.** Chartered GOCCs are created (and vested with functions) by a special law or charter and the Corporation Code only applies insofar as its provisions do not conflict with that charter.⁷ Chartered GOCCs are subject to civil-service laws,⁸ but are not required to hold annual shareholders' meetings and are not subject to minimum capital requirements. Changes to their corporate structure require amendments to their charters.⁹

General commercial laws, such as the Civil Code of the Philippines' rules on contracts and sales, apply to both non-chartered GOCCs and chartered GOCCs.

3.2.1. The importance of GOCCs in the Philippines

The rise of GOCCs in the Philippines started after World War II (Bantug, 2012, pp. 7-8^[2]). Initially, the post-war economy was driven by a national elite with its own investment interests and private banks. In 1965, however, a series of bank failures triggered the nationalisation of many financial institutions. These nationalisations, together with the martial law declared in 1972, boosted the GOCC sector and its importance (OECD, 2015^[3]). This resulted in a steady rise in the number of GOCCs: from 65 in 1970 to 303 in 1985, and 605 by August 2010 (Governance Commission for GOCC, 2016, p. 3^[4]; OECD, 2015^[3]).

In 1987, a new constitution came into force. While recognising the “indispensable role of the private sector”,¹⁰ the 1987 Constitution reaffirmed the state’s role as an economic player and conferred to Congress the power to establish “government-owned and controlled corporations [...] by special charters in the interest of the common good and subject to the test of economic viability”.¹¹ In addition, the 1987 Constitution was aimed at preventing conflicts of interest between the management of GOCCs and members of the legislative bodies.¹²

Moreover, in response to the proliferation of GOCCs over the previous two decades, a reform process was begun with Administrative Order No. 59, s. 1988, on Rationalizing the Government Corporate Sector. The reforms recognised the “need to improve the efficiency of GOCCs and their subsidiaries in order to promote economy, efficiency and effectiveness in the delivery of public services” (Governance Commission for GOCC, 2016, pp. 3-4^[4]). In 2018, the Philippines had 120 GOCCs with a total value of assets of PHP 7 916.07 billion, a net worth of PHP 3 626.28 billion and a comprehensive income of PHP 225.43 billion (Governance Commission for GOCC, 2018^[6]).

3.3. Competition law and SOEs

In 2015, the Philippines introduced the Philippine Competition Act (PCA), its first comprehensive legal framework on competition policy (OECD, 2018, pp. 167-177^[5]). The PCC, an independent quasi-judicial body mandated to implement Philippine competition policy, was established on 1 February 2016.

Section (4) of the PCA defines “entity” and includes those owned by the government directly or indirectly engaging in economic activities, meaning the act fully applies to SOEs when these perform economic activities. Indeed, in 2017, PCC investigated a complaint filed against the Philippine Health Insurance Corporation, a GOCC, for alleged anti-competitive agreements and abuse of dominant position in connection with the provision of ophthalmological services. PCC eventually closed the investigation later that year in view of the findings of its Enforcement Office and subsequent actions by the parties.¹³

In 2017, the government launched the ambitious Philippine Development Plan 2017-2022 (National Economic and Development Authority, 2017^[5]), with the objective of achieving “more inclusive growth, a high-trust and resilient society, and a globally-competitive knowledge economy”. The National Economic and Development Authority (NEDA) took the lead on this initiative and worked together with a number of public agencies, including the PCC.¹⁴

Chapter 16 of the Philippine Development Plan 2017-2022 – “Leveling the Playing Field through a National Competition Policy” – recognises that competition “makes markets perform better and promotes inclusive economic growth” and the “participation of government in providing goods and services similar to private entities [...] limits competition”.

Accordingly, PCC – in co-ordination with other agencies such as NEDA, the Department of Trade and Industry, Department of Justice, and the Governance Commission for Government-Owned and Controlled Corporations (GCG) – has the mission of formulating a National Competition Policy “to steer regulations and administrative procedures of government agencies toward promoting competition, as well as to strengthen the enforcement of anti-trust or competition laws, and effectively ensure competitive neutrality”.

3.4. SOE-specific legislation

3.4.1. Governance principles for GOCCs

After several high-profile scandals involving GOCCs, Congress passed the GOCC Governance Act of 2011, a key milestone for GOCC reform in the Philippines. The act acknowledges that while GOCCs are “significant tools for economic development”,¹⁵ new and improved policies are needed including: 1) “transparent, responsible and accountable” governance; 2) reporting and evaluation systems; 3) competent and accountable governing boards; and 4) appropriate remuneration schemes.¹⁶ The act also established GCG as the “central advisory, monitoring, and oversight body” directly attached to the Office of the President and as the entity co-ordinating state ownership.¹⁷

According to GCG, the rationale for centralising ownership also reflects the need to “balance the principle of operational autonomy in the GOCC Sector with the need for inter-agency coordination”.¹⁸ This move towards centralisation is also largely in line with OECD advice for improved efficiency in the organisation of state ownership (OECD, 2018_[6]).

GCG aims to professionalise governance and ownership of SOEs by the issuance of Memoranda Orders (MO) and Memoranda Circulars (MC) that provide standards¹⁹ and guidelines to GOCCs (such as performance indicators).²⁰ In accordance with Section 5(c) of the GOCC Governance Act, GCG adopted a Code of Corporate Governance for GOCCs²¹ and a corporate governance scorecard (CGS) for GOCCs.²² GCG also entered into Memoranda of Agreement with the Office of the Ombudsman and the Securities and Exchange Commission (SEC) regulating their mutual assistance and close co-operation.

Finally, the GOCC Governance Act echoes competitive neutrality principles, stating the need to establish “a clear separation between the regulatory and proprietary activities of GOCCs” with the aim of achieving “a level playing field” with private companies.²³ This is deemed particularly relevant in areas adequately served by the private sector.²⁴ To this end, GCG is empowered to assess whether there is a conflict between the regulatory and the commercial functions of a GOCC, and to recommend plans of action (including privatisation) to the president to solve any such conflicts.²⁵

3.4.2. GOCCs’ governing bodies

The composition of a GOCC’s board of directors depends on the company’s corporate form, as well as on its charter for chartered GOCCs. Directors may be appointed or *ex officio*.

1. **Appointed directors.** GCG prepares a shortlist of candidates that exceeds the number of directors to be appointed by at least 50%; this is then submitted to the president, who makes the appointments.²⁶ Each appointed director serves a term of one year, unless removed for cause.²⁷ According to GCG, this mechanism establishes “clear accountability lines”. GCG sets a number of requirements for appointed directors, but there are no criteria or requirements to ensure directors’ independence. For instance, in chartered GOCCs, appointed directors are not prevented from holding similar positions or other interests in the private sector, unless these are in conflict with their fiduciary duties or prohibited by a company’s charter.²⁸ For non-chartered GOCCs, the state shall nominate members of the board of directors or trustees in proportion to its percentage shareholding in the GOCC.²⁹ Additionally, the mechanism provided by the Corporation Code applies as long as these provisions are not inconsistent with the GOCC Governance Act.³⁰
2. **Ex officio directors.** The 1987 Administrative Code prescribes that “in order to fully protect the interests of the government”, at least one-third of the directors “should be a Secretary, or Undersecretary, or Assistant Secretary” (Section 42). However, this provision does not apply to chartered GOCCs with charters that prescribe a different composition of the board.

Officially, the board of directors formally selects the CEO from among its members;³¹ in practice, however, the “desired” CEO is designated by the Philippine president. The CEO should not be the chairperson, unless this is allowed by the GOCC’s charter or by-laws. The CEO’s term of office is one year, unless removed sooner for cause.³²

GOCCs’ directors are held “fully accountable to the State as its fiduciary, and act in the best interest of the State”.³³ To this end, they shall act “with utmost and undivided loyalty to the GOCC” and “with due care, extraordinary diligence, skills and good faith in the conduct of the business of the GOCC”.³⁴

According to GCG, the standards of diligence for GOCCs’ directors are stricter than the standards for directors of private companies. Moreover, GCG’s Corporate Standards Office (CSO) measures their performance through a specific monitoring system.³⁵

Directors are liable on behalf of the GOCCs, in particular for acts or omissions committed in good faith in their capacities as directors or officers. GOCCs are required to provide directors with specific insurance coverage (the Directors’ and Officers’ Liability Insurance or DOLI), sourced in general from the Government Service Insurance System (GSIS).³⁶ DOLI premiums form part of the GOCC’s operating budget and are funded by the government through the Directors’ and Officers’ Liability Fund (DOLF).

3.4.3. Disclosure requirements

GOCCs must comply with disclosure and reporting requirements as set out by GCG and other relevant laws. They are required to publish on their websites specific corporate information, including financial statements, audited reports and performance scorecards. In addition, they are required to publish specific information on “any government subsidies and net lending”, as well as “all borrowing guaranteed by the government”.³⁷

It should be noted that GOCCs are mandated to establish an internal audit function, which reports to the board audit committee, but are not required to appoint independent external auditors.³⁸ Instead, GOCCs are subject to the authority of the Commission on Audit (COA) on the expenditure of public funds.³⁹

GOCCs submit their audited financial statements to the secretary of the Department to which they are attached.⁴⁰ In addition, GOCCs submit quarterly reports and an annual consolidated report to GCG.⁴¹ GCG also prepares an annual report on the performance of GOCCs submitted to both the president and Congress, and which is made available online.

The Department of Finance monitors GOCCs’ financial performance. In particular, it carries out GOCC fiscal planning and programming. This includes the management of GOCCs’ liabilities, as well as the evaluation and approval of borrowing programmes and investment and financing plans.⁴² GOCCs periodically report to the Secretary of Finance and the Secretary of Budget on the status of obligations subject to government guarantees.⁴³ No explicit penalties are in place in case of non-compliance with reporting requirements. However, timely and accurate disclosure is one factor taken into account in the annual performance evaluation of GOCCs and which can impact on performance-based bonuses (OECD, 2017^[7]).

3.4.4. Compensation of GOCC personnel and management

The main pieces of legislation relating to the compensation of GOCC personnel and management are:

1. Executive Order No. 7 Setting Out the Guiding Principles for Compensation of GOCC Personnel.⁴⁴
2. Executive Order No. 24 Prescribing the General Rules for Directors’ Compensation; it classifies GOCCs into five asset- and revenue-based categories for determining maximum allowable compensation, and creates a compensation structure that includes a per diem component and performance-based incentives, subject to specific limitations.⁴⁵

3. Executive Order No. 36 Giving GOCCs the Option to Adopt the Modified Salary Schedule under Executive Order No. 201, which allows GOCCs' executive management to receive compensation equivalent to that being awarded by the national government and standardises various GOCCs' remuneration systems.
4. Executive Order No. 80 Harmonising the Performance-Based Incentives and Bonus Schemes for GOCCs by Adopting a Performance-Based Incentive (PBI) System.⁴⁶
5. Executive Order No. 203 Establishing a Framework for the Compensation and Position Classification System (CPCS) and the General Index of Occupation Services (GIOS) Applicable to GOCC Employees. One of this law's guiding principles is competitiveness with the private sector, particularly for GOCCs "engaged in competitive industries".⁴⁷ The framework also provides for a variable pay structure with a productivity enhancement incentive (PEI) and performance-based bonus systems.

Following these executive orders, GCG adopted a number of implementing guidelines for GOCCs, including:

1. GCG MC No. 2017-01 Relating to Performance-Based Bonuses⁴⁸
2. GCG MC No. 2016-01 Setting Out the Directors' Compensation System (DCS), a comprehensive compensation framework for members of GOCCs' governing bodies.

GCG also elaborated a dedicated compensation and position classification system (CPCS) for GOCCs in application of the Executive Order No. 203 framework. Factors relevant for setting compensation levels also include the remittance of dividends to the National Treasury, as well as the government's support to the GOCC in terms of subsidy, equity, net lending or tax subsidies.⁴⁹ One stakeholder told the OECD that a GOCC director's compensation should be published on the company's website. Nevertheless, compensation packages are often not fully disclosed and rather reported only with reference to the relevant provisions or framework.

3.4.5. Access to public resources

GOCCs are expected to generate revenue of which a share (including expenses) is given to the government and becomes part of the national budget.⁵⁰

Making explicit reference to competitive neutrality, GCG stated that the government should avoid granting advantages and benefits (such as exemptions from taxes, duties or other charges, or guarantees on debts) to GOCCs competing with the private sector, "unless justified by a greater public interest".⁵¹ The GCG determines this on "a case to case basis" after considering "the circumstances of the GOCC in relation to the public interest involved". Moreover, according to GCG, GOCCs are typically not compensated for (public) services that are offered below cost.

GOCCs are subject to income taxes,⁵² as well other taxes imposed under the revenue law pursuant to the Administrative Code of 1987. Exemptions may apply,⁵³ however, if granted by special laws or a GOCC charter.

The government can act as a guarantor of GOCCs' financial instruments, subject to approval from the Department of Budget and Management (DBM). In practice, the current leadership at the Department of Finance appears not to have provided such guarantees and, more generally, is not inclined to bail out failing GOCCs. Nevertheless, the 2019 Fiscal Risks Statement issued by the Development Budget Coordination Committee shows that outstanding government guaranteed debt to GOCCs in 2017 still amounted to PHP 489.91 billion, or 3.1% of the country's GDP, despite decreasing, while the total guaranteed debt and contractual obligations of GOCCs amounted to PHP 712.39 billion, or 4.51% of the country's GDP (Development Budget Coordination Committee, 2019^[6]). The OECD understands that none of PHLPOST's financial obligations are guaranteed by the government.

GOCCs can also get exclusive access to “programmed” subsidies upon request to the DBM. These subsidies may be provided, for instance, to expand GOCCs’ networks or existing lines of businesses.⁵⁴ Private players do not have access to these subsidies.

If a GOCC is not performing, GCG can take several actions,⁵⁵ including replacing directors, subject to the president’s approval, or recommending to the Office of the President a new capital injection⁵⁶ or investment. On a case-by-case basis, the Department of Finance may cover for the losses and would likely dispose the assets.

3.5. Transformation of GOCCs

In 2000, the Privatization and Management Office (PMO) was established as an agency attached to the Department of Finance. Assets of abolished GOCCs or unserviceable government-owned assets are assigned to the PMO, which then designs the bidding rules for privatisation.⁵⁷ Other government agencies – including GCG – can implement their own privatisation plans without requesting help from the PMO.

To support the transformation of the GOCC Sector, GCG established a Multi-Sector Governance Council⁵⁸ and later drafted *Guidelines Covering the Merger or Abolition/Dissolution of GOCCs*.⁵⁹ These guidelines prescribe that a decision to “transform” (i.e. merge, dissolve or abolish) a GOCC shall be guided by key considerations, including whether: 1) the functions of the GOCCs remain relevant or consistent with the national development policy; 2) the GOCC is still achieving the desired outcome in a cost efficient way; and 3) the GOCC is involved in activities that would be better carried out by the private sector. Under this procedure, GCG would submit a memorandum to the president, who would have to formally approve the decision.⁶⁰ Interested parties can submit to GCG requests for reorganisation, merger, privatisation or abolition of a GOCC.⁶¹

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Notes

¹ Current USD, World Bank data.

² World Bank data.

³ Section 3(o) of Republic Act No. 10149 (GOCC Governance Act of 2011). GOCCs were originally defined in Presidential Decree No. 2029 (Defining Government-Owned or Controlled Corporations and Identifying their Role in National Development); Executive Order No. 64. Executive Order No. 292 (Administrative Code of 1987) refers to corporations in which the government owns at least 51% of the capital stock. For certain purposes, GOCCs may also include: 1) financial institutions or corporations in which the government directly or indirectly owns the majority of the capital stock (government financial institutions or GFIs); and 2) instrumentalities or agencies of the government vested with special functions and endowed with some corporate powers: government instrumentalities with corporate powers (GICP) or government corporate entities (GCE), such as the Philippines Port Authority (PPA).

⁴ Under Section 5(b) of GOCC Governance Act of 2011, GOCCs are also classified into: 1) developmental/social corporations; 2) proprietary commercial corporations; 3) government financial, investment and trust institutions; 4) corporations with regulatory functions, and 5) others as may be classified by GCG.

⁵ As amended by Republic Act 11232 or the Revised Corporation Code of the Philippines.

⁶ See *GSIS Family Bank v. Villanueva*, G.R. No. 210773, Jan. 23, 2019, <http://www.chanrobles.com/cralaw/2019januarydecisions.php?id=30>.

⁷ Section 30 of Republic Act No. 10149 (GOCC Governance Act) of 2011.

⁸ GOCC employees qualify as civil servants, and the terms and conditions of employment, as well as their compensation, are fixed by law; see, Administrative Code of 1987 (Title I, Subtitle A, Chapter 2, Sections 3-4).

⁹ Chartered GOCCs can establish non-chartered subsidiaries.

¹⁰ Article XII, Section 20 of the 1987 Constitution. GCG implements this principle in the Ownership and Operations Manual Governing the GOCC Sector (GCG MC No. 2012-06). The State Ownership Policy

(Article 4) states that GOCCs shall refrain from engaging in activities adequately serviced by the private sector.

¹¹ Article XII, Section 18 of the 1987 Constitution: “the State may, in the interest of national welfare or defense, establish and operate vital industries”.

¹² In particular, it declares the incompatibility between an office or employment in GOCCs and 1) senators and members of House of Representatives; 2) the president and members of his or her cabinet; and 3) candidates who have lost elections within one year. These individuals are also prevented from holding any direct or indirect financial interest in GOCCs. The Administrative Code of 1987 and the Local Government Code (Section 94) contain similar limitations.

¹³ See <https://phcc.gov.ph/closure-investigation-alleged-violation-entities-philippine-competition-act-provision-ophthalmological-services/>.

¹⁴ PCC is also involved in the negotiations of trade agreements such as the Philippine-Japan Economic Partnership (PJEPA) and the Regional Comprehensive Economic Partnership (RCEP) promoting the principle of competitive neutrality (see Balisacan (n.d.^[7])).

¹⁵ Section 2 of GOCC Governance Act of 2011.

¹⁶ Section 2 of GOCC Governance Act of 2011.

¹⁷ Section 5 of GOCC Governance Act of 2011. Prior to 2011, oversight functions of GOCCs were assigned to ad hoc decentralised bodies.

¹⁸ GCG MC No. 2013-03 (Re-issued).

¹⁹ Under Section 5(c) of GOCC Governance Act of 2011, these standards “shall be no less rigorous than those required by the Philippine Stock Exchange or the Securities and Exchange Commission of listed companies”.

²⁰ Under Section 6 of Republic Act No. 11032 (“Ease of Doing Business Act”), GOCCs are required to set up their service standards, known as the Citizen’s Charter, “in the form of information billboards which shall be posted at the main entrance of offices or at the most conspicuous place, in their respective websites and in the form of published materials written either in English, Filipino, or in the local dialect”.

²¹ GCG MC No. 2012-07.

²² GCG MC No. 2015-07.

²³ Section 2(g) of GOCC Governance Act of 2011.

²⁴ Article 4.2 of GCG MC No. 2012-06.

²⁵ For instance, in 2017, GCG recommended the privatisation of the Philippine Amusement and Gaming Corporation (PAGCOR); this recommendation is still under review.

²⁶ Section 15 of GOCC Governance Act of 2011. The requirements for appointed directors are developed in GCG MC No. 2012-05 on Fit and Proper Rule for Appointive Directors and CEOs of GOCCs and GCG MC No. 2012-04 (4th issue) on Nomination and Appointment of Appointive Members of the Board of Directors/Trustees of GOCCs, Subsidiaries and Affiliates.

²⁷ This mirrors term limits imposed upon companies governed by the Corporation Code (see Section 22).

²⁸ GCG MC No. 2016-01.

²⁹ Section 3(b)(2) of RA 10149.

- ³⁰ Section 30 of Republic Act No. 10149 (GOCC Governance Act) of 2011.
- ³¹ Section 18 of GOCC Governance Act of 2011.
- ³² GCG MC No. 2012-09 (Third Issue); see, in particular, Sections 4.1 and 6. The board of directors may replace the CEO (even without cause) with another board member; the removed CEO remains a director.
- ³³ Section 2 of GOCC Governance Act of 2011.
- ³⁴ Section 19 of GOCC Governance Act of 2011.
- ³⁵ CGC MC No. 2014-03.
- ³⁶ Liabilities arising from fraud, breach of fiduciary duty or unethical conduct are not covered by DOLI.
- ³⁷ Section 25 of GOCC Governance Act of 2011.
- ³⁸ Under Section 26 of GOCC Governance Act of 2011, the chairman of GCG may order an audit by independent auditors, when authorised by law.
- ³⁹ Article IX(D), Section 2(1) of the 1987 Constitution. See also Title I, Subtitle B, Chapter 4, Section 11 of the Administrative Code of 1987.
- ⁴⁰ This shall occur within 60 days after the close of the fiscal year. Pending submission, GOCCs are required to operate under the previous year's budget (see Section 38 of the Administrative Code).
- ⁴¹ GCG can validate these reports through on-site visits and random sampling.
- ⁴² Article 8.4 of GCG MC No. 2012-06.
- ⁴³ Book VI, Chapter 4, Section 30 of the Administrative Code of 1987.
- ⁴⁴ Section 7 of Executive Order No. 7, s. 2010; it also established a Task Force on Corporate Compensation.
- ⁴⁵ Section 11 of Executive Order No. 24.
- ⁴⁶ Section 5 of Executive Order No. 80, s. 2012. No additional funds are allocated for GOCCs for such purpose. In addition, Section 13 of GCG MC No. 2017-03, implementing Executive Order No. 36, s. 2017 states that GOCCs shall not source funds for salaries and other compensation of personnel from government subsidies.
- ⁴⁷ See also Section 2(b) of Executive Order No. 7, s. 2010.
- ⁴⁸ Section 6 of GCG MC No. 2017-03 excludes subsidies treated as revenues in calculating the "total comprehensive income" for determining a GOCC's profitability.
- ⁴⁹ Section 7, Executive Order No. 7, Series of 2010.
- ⁵⁰ Title XVII, Chapter 1, Section 1 of the Administrative Code of 1987.
- ⁵¹ Article 11 of GCG MC No. 2012-06.
- ⁵² Section 1 of Republic Act No. 9337, amending Section 27(c) of the 1997 NIRC. [DOF-PMO] In *Bloomerry Resorts and Hotels v. Bureau of Internal Revenue*, the Supreme Court identified under what conditions GOCCs may be exempted from certain taxes.
- ⁵³ Book VI, Chapter 3, Section 20 of the Administrative Code of 1987.

⁵⁴ They would not be considered as GOCC income and would be returned to the National Treasury if they were not fully utilised.

⁵⁵ In 2012, GCG dissolved and liquidated PHLPOST Leasing and Financial Corporation (PLFC), a subsidiary of PHLPOST, because it had failed to submit financial statements and quarterly reports for three years (see GCG Memorandum Order No. 2012-22).

⁵⁶ If capital is fully subscribed and paid up, GCG would recommend increasing the authorised stock capital.

⁵⁷ PMO may contemplate partial privatisations, with certain GOCCs' businesses being carved out prior to privatisation. So far, there has been no partial privatisation of GOCCs, but this scheme is currently under consideration by GCG.

⁵⁸ GCG MC No. 2013-04.

⁵⁹ GCG MC No. 2015-03.

⁶⁰ Sections 2.6 and 2.7 of GCG MC No. 2015-03.

⁶¹ The requirements and the procedure for these requests are detailed on GCG's website.

4 Small-package delivery services in the Philippines

4.1. Economic overview of the logistics sector: a focus on small-package delivery services (SPDS)

4.1.1. Competition in the postal sector

Postal services are a form of transportation or communication service for delivering goods and information from one point to another. Postal operators compete with firms offering a variety of delivery or communications services, including, most importantly, telecommunications services. Postal services differ from other physical delivery services due to the large volume and the nature of letters and other goods they deliver; this allows them to take significant advantage of economies of scale and scope in delivery (OECD, 1999^[1]).

In many countries, an incumbent postal operator benefits or has benefited in the past from a monopoly over the handling of certain classes of mail, usually defined as mail items below a certain weight or price, or both. The primary reason for this protection of certain areas from competition is the need to preserve the internal cross-subsidisation that finances non-commercial PSO. This allows the operator to maintain service quality on unprofitable high-cost or low-volume delivery routes when other concerns, such as the obligation to maintain geographically uniform prices, limit its ability to raise prices (OECD, 1999^[1]).

This type of cross-subsidisation – using revenues from commercial activities for the non-commercial and non-profitable activities – is threatened by increasing competition. When introducing or increasing competition, countries must consider other mechanisms for the provision of any non-commercial services that need to be maintained. A variety of competitively neutral methods exist for financing non-commercial obligations, which do not threaten competition (OECD, 1999^[1]).¹

For many incumbent postal operators, the often non-regulated or less regulated and commercially attractive activity of delivering small packages to consumers has been one of the main means through which non-commercial activities have been cross-subsidised. Moreover, the drastic decline in the volume of traditional letters and postcards due to electronic communications, which has been observed in many countries around the world, continues to increase the commercial importance of small-package delivery services for incumbent postal operators.² Combining commercial and non-commercial activities should not, however, provide the incumbent postal operator with a competitive advantage in relation to its competitors in an openly competitive market.

4.1.2. Definition of a small package

There are various definitions of “small package” in the logistics industry. One method is its weight, with the upper limit determined by how much a single person can handle without using any specific equipment. Different market participants use different weight limits,³ but a commonly used upper weight limit is 31.5 kg

for a package. A separate category called “parcels” also exists, which is often used to identify packages with a weight of up to two kilogrammes within the framework of the Universal Postal Union (UPU).⁴

In the Philippines, packages are identified as: 1) small packets, with a weight of up to 2 kg or up to 5 kg; 2) small packages, with a weight of up to 20 or 35 kilogrammes, depending on agreements with postal operators in different countries; or 3) parcels, which are packages with a weight of up to 20 kg.⁵ PHLPOST determines what falls under “parcel” for internal regulatory purposes; other players active in the Philippines adopt different classifications.⁶

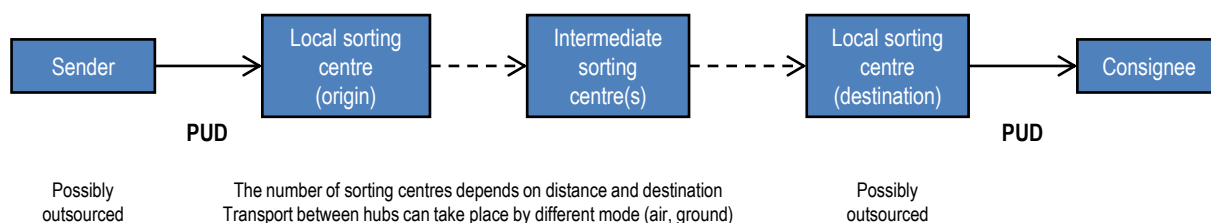
Small-package delivery services (SPDS or courier services) refer to the delivery of small packages from a pick-up location to a drop-off (delivery) location.⁷ These services are mainly segmented into: 1) express and deferred (or non-express); 2) domestic and international; 3) business-to-business (B2B) and business-to-customer (B2C); or 4) transport by air, transport by land and transport by sea. In the Philippines, to date, courier services are not defined by weight upper limit, but based solely on delivery method.

4.1.3. SPDS market structure and value chain

The SPDS industry is made up of companies that transport small packages from one location to another. An important feature of this market is that packages are picked up at an origin and delivered to destination. Known as pick-up and delivery (PUD), this involves vehicles transporting small packages from senders to consignees, through local centres and final-stage sorting facilities. Another important feature of the industry is the ability to track a shipment at every step of the delivery process.

A package moving from sender to consignee will pass through a varying number of “nodes” before reaching its final destination.⁸ Small-package delivery is inherently multimodal, using small trucks, cars or messengers for pickup and delivery and other modes of transport such as truck, rail or air for longer distances (Dennis, 2011^[2]).

Figure 4.1. Overview of steps in a small-package delivery service



Source: OECD analysis based on EC merger case COMP/M.6570 – UPS/ TNT Express, 30/1/2013 and Dennis, W.T. (2011^[2]), *Parcel and Small Package Delivery Industry*, CreateSpace, North Charleston, NC.

Different actors are active in the SPDS value chain, roughly split between integrators and non-integrators.⁹

An integrator has operational control over the SPDS logistical chain from origin to destination (including air transport), so that it can ensure delivery to meet a time commitment. The global integrators are FedEx/TNT, DHL and UPS.

There are several types of non-integrators active in the SPDS value chain.

- 1. Incumbent postal operators.** In many countries, the incumbent domestic postal operator is active in domestic and international small-package delivery. Generally, declining mail volumes have forced these operators to develop new business areas such as logistics, and in particular, SPDS.¹⁰

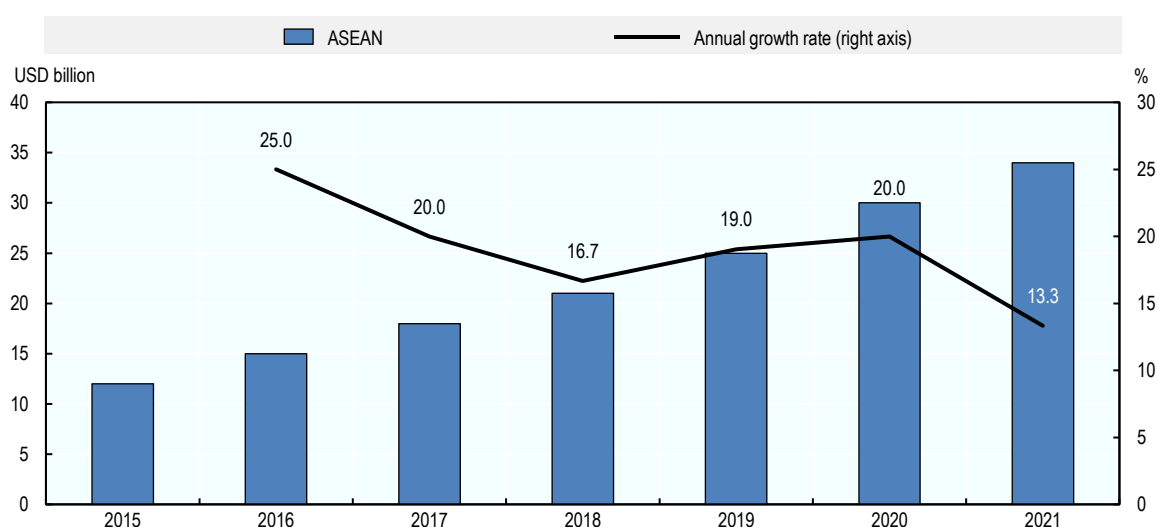
2. **Regional, national or local SPDS companies and partner networks.** These are often concentrated in the domestic small-package market. They may form alliances and partner networks to offer wider-ranging SPDS and expand into neighbouring countries.
3. **Smaller companies** with a domestic PUD ground service in one or more countries.

Many SPDS operators, both in Europe and ASEAN, offer ancillary services as a way of diversification, including warehousing and value-added services, such as quality-control service, packaging, labelling and tagging.¹¹

4.1.4. E-commerce growth and its impact on the SPDS sector

The advent and rapid growth of e-commerce has contributed to the rapid growth in demand for postal and courier services, which are responsible for the transportation and delivery of the package and some (or all) of the fulfilment activities.¹² The e-commerce market in ASEAN remains relatively small compared to other regions of the world,¹³ but by 2021 is expected to have grown at a double-digit pace with a compound annual growth rate of 19% since 2015 (see Figure 4.2). This may be a conservative estimate, as a recent study reported that in 2019 the Southeast Asian e-commerce market was worth USD 38.2 billion, and predicted that it would grow to USD 153 billion by 2024, at a compound annual growth rate of 39% between 2015 and 2024 (Google, Temasek and Bain & Company, n.d.^[3]). E-commerce revenue in the Philippines was estimated at USD 970 million in 2019 (Statista, n.d.^[4]).

Figure 4.2. E-commerce market value in ASEAN, 2015-21



Source: OECD (2018^[5]), *Economic Outlook for Southeast Asia, China and India 2018 – Update: Promoting Opportunities in E-commerce*, <http://www.dx.doi.org/10.1787/9789264302990-en>.

Globally, cross-border e-commerce transactions between businesses (B2B), as well as between businesses and consumers (B2C), have introduced new dynamics to international trade, transforming value chains and requiring logistics companies to change their business models.

In ASEAN, the rapid increase in the scale of e-commerce – and so the concomitant rise in the importance of SPDS – is being driven by multiple factors including: 1) rising levels of the use of information and communications technology (ICT); 2) the development of ICT infrastructure; 3) transportation infrastructure and logistics capabilities; 4) the use of e-commerce payment systems; and 5) the legal and regulatory

environment (OECD, 2018^[6]). Ensuring a level playing field and stimulating competition plays a crucial role when optimising the legal and regulatory environment.

ASEAN adopted the *Work Programme on Electronic Commerce 2017-2025*¹⁴ on 7 September 2017 and ASEAN Economic Ministers signed the ASEAN Agreement on Electronic Commerce on 12 November 2018.¹⁵ Both show that ASEAN has recognised the potential of the digital economy, and the need to develop the region's e-commerce industry by creating a conducive environment for its growth through advancing trade rules and building up greater digital connectivity in the region.

4.2. Competitive landscape of the SPDS sector

The SPDS market in the Philippines is open to competition. A number of third-party logistics companies (3PLs) are active in the market, including both local and regional players (mainly in Luzon Island) focusing on domestic B2C express delivery services. These include iSend, GrabExpress, GoMoto, Cliqship, JRS Express, Back Arrow Express, LBC Express, 2Go Supply Chain, Ninja Van, CheckMeOut, and Del Asia.¹⁶

The *PHLPOST Roadmap to 2020* provides estimated market share in 2012 of the different players in, what the report calls, the express delivery services (EDS) market (PHLPOST, n.d.^[6]). LBC led the market (25.96%), followed by 2Go (21.96%), JRS Express (15.98%), Air21 (14.98%), PHLPOST (12.41%), and others (8.70%). In 2019, market participants interviewed by the OECD indicated that the main service providers were: 1) JRS Express (approximately 30% market share); 2) LBC Express (approximately 20%); and 3) PHLPOST (approximately 15%). Lalamove and GrabExpress rank fourth and fifth in this segment. In the B2B segment, DHL is the strongest player, while LBC Express is the market leader for deliveries to remote areas thanks to its extensive network.¹⁷

In contrast, in 2012, the market for international express delivery services in the Philippines was dominated by the global integrators (DHL,¹⁸ FedEx/TNT and UPS), which had a combined market share of approximately 94% (PHLPOST, n.d.^[6]). Although more recent numbers are not readily available, some market studies indicate that this dominance appears to still be in place.¹⁹

Besides 3PLs, some brick-and-mortar retailers are entering the logistics market. For instance, SM Investments Corporation (SMIC or SM Group) acquired a 34.5% stake in 2GO. The SM Group is one of the largest conglomerates in the Philippines and the country's dominant player in retail with over 200 stores nationwide. Moreover, Ayala Corporation and the Global Fashion Group unveiled a plan to launch a joint-venture logistics company, Entrego Fulfillment Solutions.²⁰ Finally, several e-commerce companies are operating their own delivery services.

PHLPOST has the largest network in the Philippines with 3 offices of exchange, 9 mail-distribution centres, 62 sub-distribution centres, and 1,355 post offices (PHLPOST, n.d.^[6]). LBC Express, which operates mainly land and air transport, ranks second with 13 distribution centres and 280 hubs; it has a growing presence in emerging towns, a fleet of more than 1,500 trucks and uses "nautical highways" (i.e. road transport and roll-on roll-off vessels). Retail outlets for courier services are strategically located in high-traffic areas unlike post offices.

4.3. Sector regulation

Until 2015, the Department of Transportation and Communications (DOTC) had the power and authority to regulate courier services under Section 25 of the Postal Service Act and Presidential Decree No. 240.²¹ In 2015, the Republic Act No. 10844 (DICT Act) created the Department of Information and Communications Technology (DICT) and transferred the power and authority to regulate courier services to the Postal Regulation Division of DICT (DICT-PRD). According to its objectives, DICT-PRD ensures: 1) universal access to quality, affordable, reliable and secure services; 2) the availability and accessibility

of ICT services in areas not adequately served by the private sector; and 3) consumer protection, the fostering of competition and growth of the ICT sector.²² DICT is also tasked with improving public access by setting regulations for infrastructure in unserved and underserved areas.²³ In addition, under Section 2(f) of the Implementing Rules and Regulations of the DICT Act, DICT shall promote a “level playing field” in the sector.

Two elements of the sectoral regulation relate particularly to SDPS: licensing and price regulation.

4.3.1. Licensing

To operate in the Philippines, SPDS providers must obtain a private courier license (or franchise) from DICT-PRD.²⁴ According to information from stakeholders, applicants must meet certain legal and commercial requirements, including having warehousing facilities. DICT-PRD can either grant a national licence or a regional licence (limiting companies to one of the 16 regions). International providers also need a licence for direct operation of last-mile deliveries within the Philippines.

The requirements for granting a license are contained in DOTC’s Department Circular No. 2001-01, which was later adopted by DICT through Department Order No. 2017-001 (the original licensing guidelines). OECD was informed, however, that the earlier orders have been removed from public access as the specific licensing requirements are currently under review.²⁵

Information provided by DICT-PRD shows that licences are initially granted for one year, renewable annually for another year. From the fifth year, renewals are valid for five years. Licensees can deliver any content as a licence is not sector specific; it does appear non-transferable, however, and can be revoked, at least in theory. LBC Express told the OECD that the licensing requirements and process are not particularly burdensome. DICT has noted that the process can be completed in between one to two months. Renewal of the license, assuming a complete submission of the required documents, requires on average 10 to 15 days, according to DICT.

As of 1 December 2019, DICT listed 110 authorized private express and/or messengerial delivery services (PEMEDES) or courier service providers on its website.²⁶ Stakeholders noted that due to the existence of a large number of licensees in the Philippines, there is an informal moratorium on the granting of new licences and the treatment of applications to extend the geographical scope of existing licences as new applications. This moratorium was introduced in 2006 and prolonged under DICT’s authority well beyond the “transition period”.²⁷ As a result, in practice, many licences that were granted to now “dormant companies” are traded on a secondary market, even though they are not transferable. In addition, approximately 50 to 70 players are operating without a licence. These practices are at least partially a consequence of the protracted moratorium, and they indicate that, even though DICT-PRD can issue cease and desist orders against service providers operating without a licence,²⁸ its enforcement actions are extremely limited.

4.3.2. Price regulation

Under Sections 26 and 27 of the Postal Service Act, DICT-PRD has the authority to establish minimum rates for the delivery of mail and small packages. DOTC Circular No. 2001-01, currently under evaluation by DICT, describes the process for the calculation of minimum rates. DICT-PRD has stated that a revised regulation – likely to maintain the minimum-rates mechanism – would be released during the first half of 2019; to date, this regulation has not been made available.

Based on information provided by DICT-PRD, the minimum rates – revised in 2014 – are supposed to be calculated “in coordination with PHLPOST, the National Economic Development Authority (NEDA) and the Bangko Sentral ng Pilipinas” (Central Bank of the Philippines). In practice, PHLPOST itself determines the rates and DICT-PRD formally approves them. Licensed service providers must comply with them and DICT-PRD can conduct inspections to monitor compliance.

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Notes

¹ One option is raising funds for universal service through charges, such as taxation or a levy, on all postal operators.

² See, for example, EC (2018_[7]).

³ European Commission Case M.6570 – UPS/ TNT Express, paragraphs 36-39, and European Commission Case M.7630 – FEDEX / TNT EXPRESS, paragraphs 78-80.

⁴ Established in 1874, the Universal Postal Union (UPU) is a specialised agency of the United Nations. With 192 member countries, the UPU is the primary forum for co-operation between postal-sector participants. The UPU helps to ensure a truly universal network of up-to-date products and services, sets the rules for international mail exchanges, and makes recommendations to stimulate growth in mail, parcel and financial services volumes and improve quality of service for customers.

⁵ In addition, for express delivery services, Universal Postal Union guidelines prescribe a weight of up to 30 kg, which is increased to up to 35 kg under bilateral agreements such as between the Philippines and

South Korea. To address the e-commerce demand, the Asian Pacific Postal Union (APPU) created a new APPU packet classification for small packages with a weight from 0.1 to 3 kg.

⁶ For instance, LBC Express over-the-counter service is limited to 30 kg.

⁷ For an analysis of the value chain of SPDS, see European Commission Case M.7630 – FEDEX / TNT EXPRESS, para 28 and ff.

⁸ A node is a connection point within a network. See, EC merger case COMP/M.6570 – UPS/ TNT Express, 30/1/2013, recital 44.

⁹ The European Commission defines integrators using five basic characteristics: 1) ownership of or full operational control over all transportation assets, including an air network with scheduled flights, through which a large proportion of the volumes handled by the company is carried; 2) sufficient global geographic coverage; 3) a hub-and-spoke operating model; 4) a proprietary IT network that allows all relevant data to run across one network; 5) a reputation for reliably delivering parcels on time (so-called “end-to-end credibility”).

¹⁰ See EC merger case COMP/M.7630 – Fedex / TNT Express, 08/01/2016, recital 28 and further. Several postal operators had changed their focus from the traditional mail business to small-package, e-commerce-based companies with cross-border presences. Examples include Deutsche Post, Royal Mail, PostNL, Swiss Post, Estonian Post, Correos, Bpost, Österreichische Post and PostNord, which are upgrading or have upgraded their offer in order to meet new demands, particularly in the B2C segment.

¹¹ Integrators or larger SPDS operators may outsource certain elements of the value chain to outside service providers (OSP), which generally perform pick-up, delivery and certain sorting functions for small-package companies. This is often on a branded basis, so that the customers are not aware that an OSP is a subcontractor. An authorised service contractor (ASC) is typically a small-package company within a particular region – usually a single country – that enters into direct relationships with the customer in that country of its own account. An ASC may also be integrator branded, in which case the vans and drivers usually carry the brand of the integrator on their trucks, paperwork and uniforms, so customers may not realise that the ASC is an independent company.

¹² The definition of e-commerce used in this report is taken from the OECD Glossary of Statistical Terms (<https://stats.oecd.org/glossary/detail.asp?ID=4721>): “An e-commerce transaction is the sale or purchase of goods or services, conducted over computer networks by methods specifically designed for the purpose of receiving or placing of orders. The goods or services are ordered by those methods, but the payment and the ultimate delivery of the goods or services do not have to be conducted online. An e-commerce transaction can be between enterprises, households, individuals, governments, and other public or private organisations”.

¹³ In 2018, the ASEAN e-commerce market accounted for approximately 1% of worldwide e-commerce revenue. See OECD (2018^[5]).

¹⁴ See <https://cil.nus.edu.sg/wp-content/uploads/2019/02/2017-2025-ASEAN-WP-e-Commerce.pdf>.

¹⁵ See <http://agreement.asean.org/media/download/20190306035048.pdf>.

¹⁶ See www.sulit.ph/blog/11-same-day-delivery-couriers-in-the-philippines.

¹⁷ B2B accounts for 40% of LBC Express’s business. The company also offers warehousing space to customers including Samsung and Sony.

¹⁸ DHL is now operating in different segments with three subsidiaries: DHL Global, DHL Supply (B2B), and DHL Express (domestic). DHL and LBC Express are now in a formal partnership that sees LBC Express

delivering in the domestic markets where DHL is not present and DHL delivering overseas on behalf of LBC Express.

¹⁹ See, for instance, GlobeNewswire (2019^[8]): “The express delivery market in the Philippines is largely dominated by four key global players namely DHL, FedEx, United Parcel Service and TNT Express which collectively contribute to the majority of revenues in the international express delivery market in the country during 2017”.

²⁰ See www.portcalls.com/ayala-corp-enters-logistics-business-with-entrego.

²¹ Republic Act No. 7354 (Postal Service Act or Charter). The Civil Aeronautics Board (CAB) regulates air transport and the Department of Transportation (DIT) regulates land and sea transport.

²² Section 2(e) and (n) of the DICT Act.

²³ Section 6.II (d) of the DICT Act.

²⁴ Before 2015, the Licence was granted by DOTC.

²⁵ DOTC Circular No. 2001-01 (Rules and Regulations in the Processing, Hearing and Adjudication of Applications for Authority to Operate Private Express and/or Messenger Delivery Service, and in Investigation of Complaints in connection with the Operation of such Services). As of December 2019, consultations on the revision of the postal service rules were ongoing. See <https://dict.gov.ph/extension-notice-conduct-of-consultations-on-revising-and-updating-the-postal-service-rules-and-regulations>.

²⁶ DICT List of Authorized Private Express and/or Messengerial Delivery Service (PEMEDES) or Courier Service Providers as of 1 December 2019, <https://dict.gov.ph/list-of-authorized-pemedes-or-courier-service-providers-2019>.

²⁷ Section 19 of the DICT Act prescribed a transition period of six months; this should have expired on 23 November 2016.

²⁸ Section 26 of the Postal Service Act.

5 PHLPOST and its impact on competition in SPDS

5.1. The SOE active in the SPDS sector: PHLPOST

PHLPOST is a chartered GOCC established in 1992 by the Postal Service Act, which serves as its charter. PHLPOST is wholly owned by the state and does not operate or control any subsidiaries.

Until 2011, PHLPOST was an agency attached to the DOTC and the Commission on Information and Communication Technology (CICT). Under Executive Order No. 47, s. 2011, CICT was renamed the Information and Communications Technology Office (ICTO) and PHLPOST was “retained” – and currently remains – under the direct jurisdiction of the Office of the President (PHLPOST, n.d.^[1]). The GOCC Governance Act of 2011, which in part supersedes the Postal Service Act, and civil-service laws apply to PHLPOST.¹

Section 9 of the Postal Service Act allows for the possibility of private investors acquiring PHLPOST shares and establishes two classes of shares: Class A and Class B of equal par value. Only the government can subscribe for Class A shares, while Class B shares – available to private investors – cannot exceed 55% of PHLPOST’s capital.² However, currently no Class B shares have been issued as PHLPOST is fully owned by the state.

Further, PHLPOST has already been included for several years on the Department of Finance’s list of Assets for Disposal (PMO, 2017, p. 25^[2]).³ In the past, concrete steps were taken to privatise PHLPOST, but employees opposed the plan, and – most importantly – the external advisors evaluating PHLPOST were unable to finalise their assessment due to a lack of accurate corporate information. According to some stakeholders, no current privatisation plan is currently in place.

5.1.1. PHLPOST’s activities

PHLPOST is the designated postal operator for the Philippines’ UPU obligations and operates in three business areas: 1) mail services, offering mail, letter post and parcel post; 2) express and logistics services, offering express post, logistics and warehousing services; and 3) payment and retail services, offering retail collection services, postal identification cards, sale of philatelic stamps and merchandise (PHLPOST, 2017^[3]). PHLPOST is not active in the operation and leasing of warehouses. Following a 2013 rationalisation plan,⁴ PHLPOST reduced its workforce from 12 727 positions (of which 9 979 were filled) to 7 676 positions (of which 7 043 were filled).

In 2017, PHLPOST’s revenue amounted to PHP 3 536 million. Domestic ordinary and registered mail delivery services made up almost half of its revenue (48%), while express and logistics services accounted for 32% (see Figure 5.1) (PHLPOST, 2017^[3]).

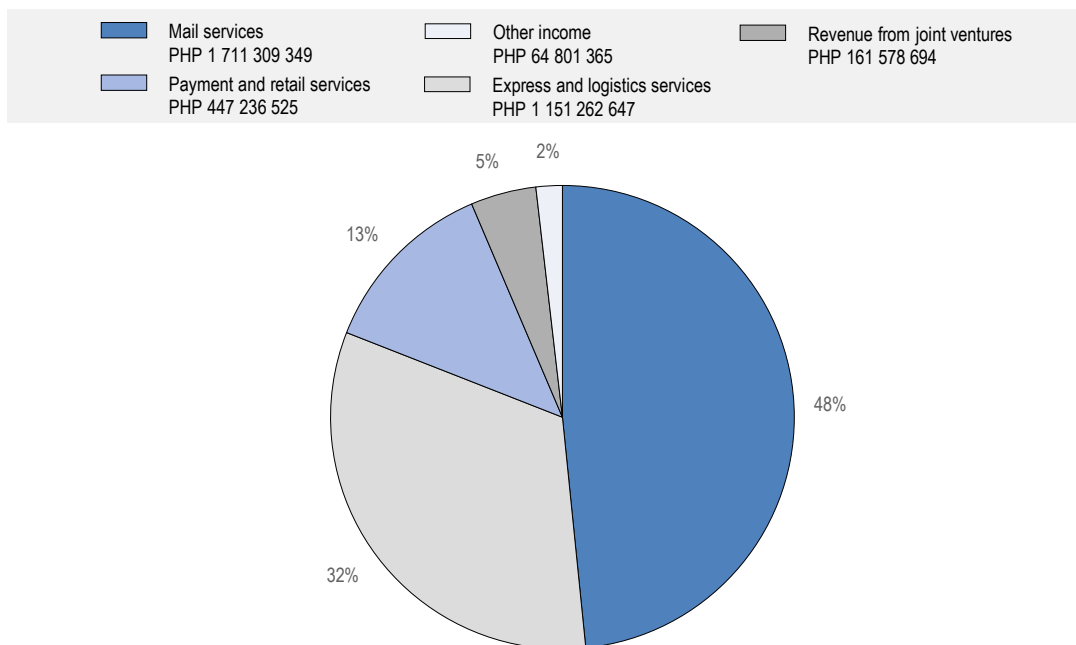
Changes in the business environment and the continuing constant decline of mail volumes due to new technologies have had a negative impact on PHLPOST's financial performance, resulting in the company's increased focus on logistics and e-commerce business (PHLPOST, 2017^[3]).⁵

5.1.2. Mandate

Section 3 of the Postal Service Act states that the delivery of letters and other mail matters is “a basic and strategic public utility which the State shall provide, directly or indirectly”. On that basis, it is PHLPOST's responsibility to deliver mails and parcels “throughout the Philippines”, as well as to develop and operate a network that “extends or makes available, at least ordinary mail service, to any settlement in the country”.⁶

To reflect its mandate, PHLPOST envisages being the “Universal Delivery Service Provider of quality-driven communications, goods and merchandise [...] in every Filipino community by 2022” (PHLPOST, 2017^[3]).

Figure 5.1. PHLPOST Revenue 2017 (in PHP)



Source: PHLPOST (2017^[3]), *PHLPOST 2017 Performance Report – 2017 Highlights of Accomplishments*, www.phlpost.gov.ph/files/corporate_governance/Annual%20Report%202017%20Highlights%20only.pdf.

5.1.3. Oversight and management

As noted in Section 2.4.1, the GOCC Governance Act of 2011 applies to key aspects of PHLPOST's governance, such as the appointment of directors, their remuneration, performance evaluations, and performance audits.

PHLPOST's significant impact upon the national budget means it is overseen by GCG and closely monitored by the Department of Finance, which can intervene in the GOCC's investments.⁷

PHLPOST's decision-making body is a board of directors composed of seven members, including the Postmaster General who also serves as the corporation's CEO. PHLPOST directors are appointed by the president;⁸ it has no ex officio directors.

5.1.4. SPDS business

As described in Section 3.2, PHLPOST has one of the largest networks in the Philippines and operates both non-express (postal) services and express (courier) services.⁹ For domestic express mail delivery, PHLPOST relies on land transport (and on air transport for specific areas). Following COA's rules on hiring contractors, PHLPOST outsources sea and air transport services and occasionally road transport services, despite it having a fleet of approximately 380 vehicles.¹⁰

PHLPOST indicated that between the two main cities Manila and Cebu, maximum delivery time is two days. For remote areas with no postal facilities, PHLPOST's door-to-door delivery service for parcels is replaced with the delivery of pick-up information.

PHLPOST's performance is evaluated through a scorecard agreed between the corporation and GCG¹¹ and it has to submit quarterly monitoring reports to GCG.¹² These two evaluations show that in 2017 PHLPOST had an average efficiency rating – including for SPDS – of 90%, with 98% of its parcels delivered within seven days (PHLPOST, 2017^[3]). In 2018, PHLPOST reported a GCG rating of 80.49%, with 94.75% of international parcel post deliveries delivered within seven days. While benchmarking is important to improve assessments of PHLPOST's performance (OECD, 2015, p. 41^[4]), the reported data are the result of self-assessment and do not take into account the performance of its competitors.¹³ Comparison or benchmarking of their performance with some of their competitors or peers could provide a context for or help interpret PHLPOST's performance.

Notwithstanding its efficiency rating in the performance scorecard and its competitive rates both for the retail and corporate markets (PHLPOST, n.d.^[1]), PHLPOST does not have a strong reputation for small-package express delivery.¹⁴ In addition, based on interviews with stakeholders, it is widely accepted that online sellers and large customers seem reluctant to use PHLPOST because it is not considered reliable.¹⁵

5.2. Assessment of PHLPOST's advantages and disadvantages in the SPDS sector

This section identifies and assesses PHLPOST's advantages and disadvantages in the SPDS sector, and offers recommendations to address these issues. Each sub-section commences by setting out the general principles guiding the assessment; these are mainly taken from the *OECD Guidelines on Corporate Governance of State-Owned Enterprises* (OECD, 2015, p. 20^[4]).

5.2.1. PHLPOST's public-service obligation (PSO)

General principles

Costs related to public-policy objectives should be funded by the state and disclosed.

Where SOEs combine economic activities and public-policy objectives, high standards of transparency and disclosure regarding their cost and revenue structures must be maintained, allowing for an attribution to main activity areas.

SOEs' economic activities should be required to earn rates of return that are, taking into account their operational conditions, consistent with those obtained by competing private enterprises.

PHLPOST is responsible for the delivery of letters and parcels “throughout the Philippines”, as well as for developing and operating a network that “extends or makes available, at least ordinary mail service, to any settlement in the country”.¹⁶ In essence, this provision results in a PSO.¹⁷ There is no secondary legislation or separate law regulating PSO.

Although the Postal Service Act refers to “at least ordinary mail”, in practice, this obligation extends to small packages, which fall under the definition of “letters”.¹⁸ Consequently, PHLPOST is the only SPDS provider committed to delivering to the whole country; its competitors can take commercial and strategic decisions on the areas to serve (and often apply for licences limited to those areas).

According to internal estimates, deliveries to remote areas account for 20% of its operations, with PHLPOST being required to apply the same (standard) rates. PHLPOST does not consider the delivery of small packages to remote areas to be cost-effective, yet receives no compensation from the government.¹⁹ These services are cross-subsidised by the revenue that PHLPOST generates in Manila and other key urban areas.²⁰ GCG has indicated that, although PHLPOST has been profitable since 2012, the PSO has still an impact on its competitiveness and partially explains its low profitability.

The OECD has one recommendation.

1. PHLPOST should be adequately compensated for the fulfilment of its PSO. Based on other countries' experiences, a PSO can be funded using various methods including:
 - a. direct or indirect transfer payments from the government
 - b. granting access to PSO through public procurement or
 - c. contributions into a universal service fund from other service providers or their users (Dieke, 2016^[5]).

5.2.2. An SOE governed and managed as an arm of government

Government's influence over PHLPOST

General principles

The boards of SOEs should have the necessary authority, competencies and objectivity to carry out their functions of strategic guidance and management monitoring. They should act with integrity and be held accountable for their actions.

Notwithstanding GCG's role, the government's influence over PHLPOST seems to exceed the legitimate objectives of shareholders in private entities. Even though the ownership rights remain with the Office of the President (represented by GCG), line ministries exercise supervision over their respective GOCCs for purposes of public policy and programme co-ordination, according to GCG.²¹ These agencies may influence GOCCs in matters beyond public policy objectives especially through ex officio directors.²²

Rules and procedures for nominating and appointing a CEO should be transparent and respect lines of accountability between the CEO, the board and the ownership entity (OECD, 2015, p. 70^[4]). Although PHLPOST's board of directors formally selects the CEO (who is also the Postmaster General),²³ in

practice, stakeholders have indicated that the Philippine president may influence the nomination. This is in line with Section 4.1(a) of GCG Memorandum Circular 2012-09, which states that “preference” shall be given to the individual nominated by the president. This may result in the appointment of a CEO without sufficient competence or expertise in PHLPOST’s sector or who might be pursuing political, rather than purely commercial interests. The OECD does acknowledge, however, that this risk is partially mitigated by GCG’s Fit and Proper Rule for Appointive Directors and CEOs of GOCCs.²⁴

Any establishment of subsidiaries or acquisition of a private entity by a GOCC shall be subject to prior clearance from GCG.²⁵ Similarly, any GOCC proposal for a contractual joint venture with a private partner must be submitted to GCG for review and then through the NEDA Board Investment Coordination Committee for recommendation by the president.²⁶ PHLPOST does not yet operate any subsidiaries or joint ventures, which may be partly due to the complexity of this mechanism. According to GCG, GOCCs have requested to establish subsidiaries, but, to date, it has neither recommended or supported any requests. Although subsidiaries’ performances may have an impact on the state’s budget, there are a number of legitimate business reasons for the establishment of a subsidiary. For example, subsidiaries can improve a GOCC’s competitiveness by facilitating entry into a new business or through the provision of specialised services. Similarly, the establishment of a joint venture may often have pro-competitive effects such as combining firms’ different areas of expertise or enhancing a GOCCs’ ability to lower prices or increase output through possible new services or efficiencies created by a joint venture.

The OECD has two recommendations.

1. Transparency safeguards in the CEO selection and appointment process, and in the evaluation criteria, should be introduced to ensure that the board of directors is not unduly influenced.
2. Cases for which an ownership entity needs to obtain the president’s ex ante approval should be limited and relate only to significant transactions, such as those that are high risk or exceed a certain value.²⁷

PHLPOST’s services rendered to the state

Under Section 35 of the Postal Service Act, PHLPOST has a duty to offer its express and non-express mail delivery services to bodies and individuals holding so-called franking privilege: the right to send mail without payment of postage.²⁸

In G.R. No. 105371, November 11, 1993, the Supreme Court annulled Section 35 of the Postal Service Act that had withdrawn the franking privilege from the courts, along with certain other government offices. This Supreme Court ruling is evidence of a combination of public-service obligations and “advantages” granted to PHLPOST, which may result in market distortion. In its reasoning, the Supreme Court noted that the provisions conflicted with the equal protection clause²⁹ and, most importantly, noted that PHLPOST “was created and is expected to operate for the purpose of promoting public service”. The Supreme Court stated in its reasoning that while PHLPOST “may have been established primarily for private gain, it cannot excuse itself from performing certain functions for the benefit of the public in exchange for the franchise extended to it by the government and the many advantages that it enjoys under its charter”.

Franking-privilege funding is disclosed in PHLPOST financial statements. In 2017, the “reimbursement of Franked Mails” amounted to over PHP 536.5 million, yet no clear compensation system exists for these services. In fact, although in principle PHLPOST should be reimbursed based on costs incurred, stakeholders have noted that the National Treasury generally “negotiates” discounts with PHLPOST on the amount owed.³⁰ More particularly, PHLPOST has requested that the debt be included in the General Appropriations Act, making it part of the overall government budget, through the Department of Budget and Management. A related provision in the Local Government Code prescribes a discounted offsetting of monies owed by local government units (LGUs) to GOCCs (and assumed by the national government).³¹

To maintain a level playing field with private competitors, PHLPOST needs to be adequately and transparently compensated for the fulfilment of public policy objectives (OECD, 2012, p. 10^[6]).³² In practice, PHLPOST currently provides services to the central government and LGUs without receiving appropriate compensation. There is also no clear rule to calculate the actual costs of fulfilling the obligation. PHLPOST argues that the current amount reimbursed results in under-compensation, which affects PHLPOST's overall performance.³³

The OECD has two recommendations.

1. PHLPOST should keep separate accounts related to franking-privilege services.
2. Franking-privilege services should be adequately compensated. This might take various forms (including foregone dividends by the state), as long as it is identified and accounted (OECD, 2015, p. 47^[4]). Compensation should be detailed in legal provisions or through contractual mechanisms, rather than ex post negotiations. The contractual mechanism should take into account, for instance, the quality of franking-privilege services using objective criteria and allow for periodic adjustments that take into account any quality improvements in those services.

PHLPOST's arrangement with the Bureau of Customs

General principles

Mechanisms should be implemented to avoid conflicts of interest preventing board members from objectively carrying out their board duties and to limit political interference in board processes.

Stakeholders have submitted that it is common practice for government agencies and GOCCs to have agreements in place. For example, Section 32(b) of the Postal Service Act envisages a “working arrangement” between PHLPOST and the Bureau of Customs (BOC) for inbound and outbound deliveries. This was formalised with a first Memorandum of Agreement in 2014, which was amended in 2016. The MOA's preamble states that to enhance competitiveness and sustain operations, PHLPOST and BOC “shall cooperatively and jointly promote the development of international trade that will rationalize and simplify procedures”.

Under the Amended Memorandum of Agreement (2016), BOC was given the responsibility for providing adequate personnel to the 24/7 operations at PHLPOST's customs warehouse office.³⁴ Moreover, the parties committed to a “centralised examination and assessment of customs duties”³⁵ and to reinforce their co-operation by establishing a “joint committee”³⁶ and, within such committee, a joint “technical working group”.³⁷

Other market players, such as LBC Express and DHL, have also some arrangements with the BOC, and PHLPOST has submitted that BOC does not grant it any preferential treatment. Yet it does have at least enhanced co-operation, with BOC offering support to increase PHLPOST's competitiveness.

In practice, this arrangement appears to have limited impact on the SPDS market, with the international sector in the Philippines largely dominated by the global integrators. Nonetheless, BOC's enhanced co-operation with PHLPOST may prevent domestic and regional players from entering the international SPDS market or increase their costs

The OECD has one recommendation.

1. As a general principle, all public agencies should treat GOCCs and privately owned companies equally. For the specific relationship between PHLPOST and BOC, the Bureau should ensure

through the adoption of internal guidelines or ministerial circulars that the same levels of service and commitment are offered to all players in the SPDS market.

5.2.3. Different regulatory treatment

PHLPOST as a chartered GOCC

PHLPOST is a chartered GOCC. As explained above, the Corporation Code only applies suppletorily to PHLPOST,³⁸ insofar as this Code is not inconsistent with the Postal Service Act and the GOCC Governance Act of 2011.

PHLPOST's accounts are solely audited by the COA and no external (independent) auditors can be appointed. This has been an issue in the past of COA reportedly having insufficient resources and being seen as being part of the "public sector" (Bantug, 2012^[7]) (see Section 4.2.4). Regardless of PHLPOST's legal status, specific state control procedures do not substitute for an independent external audit. In fact, the COA monitors the use of public funds and budget resources, rather than the operations of PHLPOST as a whole.

The OECD has two recommendations.

1. The legislator should reconsider the legal form under which PHLPOST (and other chartered GOCCs) operate and incorporate them under the Corporation Code.
2. PHLPOST's financial statements should be subject to independent external audit (OECD, 2015, pp. 65-66^[4]).

Licensing requirements

Since PHLPOST's charter explicitly assigns it the right to operate SPDS, it is not required to obtain a licence.³⁹ This exemption from the licensing requirement, which is the direct result of it being a chartered GOCC, means PHLPOST does not have to meet the legal and commercial licensing requirements imposed on other service providers to operate express messenger or delivery services. It also exempts it from the annual renewal process (until the fifth year) that is required of its competitors.

The DICT-PRD moratorium that is currently preventing the issuance of new licences and permissions to extend the geographic scope of existing licences also confers an advantage to PHLPOST and other players already operating nationwide.

The OECD has one recommendation.

1. The legislator should subject PHLPOST's commercial activities, such as its courier services, to comparable licensing requirements as those imposed upon other players.

PHLPOST and the sectoral regulator

General principles

There should be a clear separation between the state's ownership function and other state functions that may influence the conditions for state-owned enterprises, particularly with regard to market regulation.

Section 6(h) of the Postal Service Act refers to PHLPOST's power to issue regulations on "postal services". While the OECD was not granted access to these "regulations", which are known as Administrative Orders, PHLPOST explained that they did not allow for the regulation of the conduct of PHLPOST's competitors and were rather PHLPOST's internal rules to improve postal systems through the adoption of international best practices.

In addition, PHLPOST's attachment to the Department of Transportation and Communications for "policy coordination" does not seem to raise any prima facie concerns.⁴⁰ However, this rather general provision may trigger misinterpretation as to the relation between DICT-PRD, the current regulator, and PHLPOST. For instance, DICT-PRD indicated that while it has only limited regulatory powers on PHLPOST, it has a "duty to protect" such GOCCs (including PHLPOST).

The OECD has three recommendations.

1. The Postal Service Act should be amended to clarify that PHLPOST does not exercise any regulatory powers over the industry.
2. The DICT Act and the Implementing Rules and Regulations of the DICT Act should explicitly state that DICT executes the regulatory role in the relevant sector.
3. The DICT Act and the Implementing Rules and Regulations of the DICT Act should explicitly state that DICT-PRD regulation equally applies to PHLPOST and its SPDS competitors.

Minimum rates

As stated above, DICT-PRD regulates last-mile delivery services and sets minimum prices for SPDS; DICT is currently revising its calculations of these minimum rates.

The scope of these minimum rates' applicability is uncertain. In particular, it is unclear whether these rates cover only ordinary domestic mail (non-tracked letters and small packets up to two kilogrammes), or whether the minimum rates apply to all courier services (parcels, international deliveries and express deliveries). Notwithstanding the uncertainty, this price regulation appears to affect the level playing field in the SPDS sector.

Rates appear to be based on PHLPOST's rates. Once DICT-PRD has approved the minimum rates, PHLPOST cannot adjust its rates, which are considered low compared to those applied by private SPDS providers.⁴¹ While PHLPOST cannot price below DICT-PRD approved minimum rates, it can offer volume-based discounts to its business customers.

By contrast, PHLPOST's competitors often disregard these minimum rates by offering customer discounts and there is no structure to monitor compliance. Indeed, these minimum rates seem to have a limited impact on PHLPOST's competitors who often charge above the minimum rates by providing premium services.

The OECD has one recommendation.

1. The legislator should consider abolishing the minimum-rates regulation. Alternatively, in its new Ministerial Circular (currently under consideration), DICT should increase transparency around the mechanism to calculate the minimum rates for SPDS, including the full list of the services and products covered by such minimum rates. Minimum rates should be based on an independent regulatory assessment, including the sector's cost structure, rather than solely on PHLPOST's rates.

5.2.4. Privileged access to public procurement markets

PHLPOST's advantages in public tenders

General principles

When SOEs engage in public procurement, whether as bidder or procurer, the procedures involved should be competitive, non-discriminatory and safeguarded by appropriate standards of transparency.

Public procurement rules apply to all public entities, although GCG and the Government Procurement Policy Board (GPPB) have yet to issue any specific guidelines on GOCCs.⁴²

GOCCs must participate in public tenders to be awarded public contracts. In order to be eligible to participate, the rules prescribe that GOCCs must be: 1) legally and financially autonomous; 2) operating under commercial law; and 3) not attached agencies of the procuring entity.⁴³

The widespread view among stakeholders is that GOCCs are seen as part of the “public sector family”. In practice, based on input received from one stakeholder, GOCCs – including PHLPOST – have three main advantages:

1. Unlike private companies, GOCCs are not required to register with the Philippine Government Electronic Procurement System (PhilGEPS).⁴⁴
2. The government and a GOCC can simply enter into a simplified “agency-to-agency” contract under the flexibility granted by the Government Procurement Reform Act, and so avoid the general requirement for a public tender.⁴⁵
3. A well-functioning, dedicated mediation process under the Secretary of Justice exists for disputes between GOCCs or between a GOCC and the government. These rulings are conclusive and binding (except in exceptional circumstances, when they are appealable to the president).⁴⁶ Moreover, the Department of Justice provides legal advice to GOCCs.⁴⁷

These advantages may significantly reduce costs (including of potential disputes) for GOCCs, including PHLPOST, and may offer an incentive for government agencies to source services from GOCCs using “agency-to-agency” contracts, rather than by holding tenders to allow participation from private providers.

PHLPOST's delivery-service contracts with government agencies generally concern mail, so the direct impact on SPDS appears to be limited. Nevertheless, the procurement rules applicable only to GOCCs do not grant non-discriminatory access to fair procurement (OECD, 2015, p. 21; 46; 50₍₄₎).

The OECD has two recommendations.

1. GOCCs, including PHLPOST, should be subject to comparable pre-accreditation requirements as those demanded of private bidders and the strict conditions under which the government can enter into “agency-to-agency” contracts with GOCCs should be clearly defined.
2. A mediation mechanism comparable to the one in place for GOCCs should be accessible to private bidders.

PHLPOST's advantages at local level

At local level, GCG indicated that PHLPOST engages personnel in LGUs and municipalities to perform last-mile delivery services; they are paid under a contract of service. Although private competitors may

enter into similar arrangements, it appears that PHLPOST has better access to LGUs due to long-standing relationships and its consolidated presence even in remote areas in the Philippines.

In rural areas, some local authorities offer space to PHLPOST to establish post offices or branches in “government centres”.⁴⁸ This space is lease-free for PHLPOST, giving it privileged access as should competitors decide to open a branch in the same area, they would have to incur costs that PHLPOST does not.⁴⁹ In certain instances, they may even be unable to access the market or establish a presence in these areas.

The OECD has one recommendation.

1. LGUs should grant access to government centres through open and fair tendering procedures, particularly where SPDS providers already operate in the area or have expressed an interest in establishing a branch.

5.2.5. Financial advantages

Government subsidies and guarantees

As a result of the GOCC Governance Act of 2011, which envisages the possibility of the government subsidising GOCCs, subject to disclosure requirements, PHLPOST has received subsidies.⁵⁰ In 2013, PHLPOST received two direct subsidies: 1) incentive benefits to employees affected by the Rationalization Plan (essentially for early retirement and “separation pay”) worth over PHP 515.6 million; and 2) a rebate on its 2012 corporate income tax and 2013 value added tax worth nearly PHP 357 million.

Based on 2017 Financial Statements, PHLPOST was granted “subsidy income” as compensation for franking-privilege services (see Section 4.2.1) amounting to over PHP 536.5 million.⁵¹ Such compensation may not technically qualify as a subsidy, however; GCG has explained that it is actually payment for the service rendered to the government and may underestimate actual costs.

Second, as indicated in Section 2.4.5, GOCCs have access to “programmed” subsidies by proposing projects as part of the state’s annual budget.⁵² PHLPOST explained that it had formally requested (and was granted) a subsidy, but funds were not released due to divergences on the conditions imposed.

Third, Section 12(e) of the Postal Service Act envisages that the government can, if necessary, act as guarantor for PHLPOST’s obligations; PHLPOST appears never to have benefited from this potential advantage. PHLPOST does appear to have requested guaranteed loans, which the Bureau of the Treasury has never approved.⁵³ Moreover, PHLPOST has neither issued bonds (or any other debt instrument) nor contracted foreign debts, subject to the Department of Finance’s approval.⁵⁴

In general, the state should not automatically guarantee GOCCs’ liabilities and any state guarantees should be properly disclosed, for which the current framework appears sufficiently transparent (OECD, 2015, p. 48; 64_[4]). Although the current government has not acted as a guarantor for PHLPOST’s liabilities, the Postal Service Act gives a legal foundation for such initiatives.

Under EU state aid rules, for instance, it is recognised that guarantees given directly by the state and guarantees given through state resources can distort or threaten to distort competition by favouring certain firms. These guarantees are assessed using the market economy investor principle, which takes into account the effective possibilities for a beneficiary firm to obtain equivalent financial resources on the market with conditions that would be acceptable for a private operator.⁵⁵

The OECD has two recommendations.

1. Section 12 of the Postal Service Act should be amended to reflect that the state will not grant any preferential financial treatment to PHLPOST.

2. The legislator could consider mechanisms, such as guarantee fees, that impose compensatory payments to the Bureau of the Treasury by GOCCs whose borrowing costs are lower than those of comparable private companies thanks to state guarantees (OECD, 2015, p. 49^[4]).

Access to finance

General principle

SOEs' economic activities should face market consistent conditions regarding access to debt and equity finance.

SOEs' relations with all financial institutions, as well as non-financial SOEs, should be based on purely commercial grounds.

Although there is no indication in the disclosed information that PHLPOST has received any direct loans from state-owned banks or financial institution, stakeholders have told the OECD that in general GOCCs deal with state-owned financial institutions, such as the Land Bank of the Philippines.

GOCCs' relations with all financial institutions should be based on purely commercial grounds. If creditors assume that lending to a GOCC carried an implicit state guarantee, this might lead to below-market funding costs. Moreover, with state-owned financial institutions, there is risk of conflicts of interest, which may lead to GOCCs accumulating excessive debt with its subsequent market distortions (OECD, 2015, pp. 48-49^[4]).

The OECD has one recommendation.

1. The legislator should ensure that PHLPOST's relations with state-owned financial institutions are on commercial grounds and should minimise the risk of conflicts of interests, such as PHLPOST's directors also sitting on the boards of state-owned banks.

Protection from takeover and bankruptcy procedures

General principle

As a guiding principle, SOEs undertaking economic activities should not be exempt from the application of general laws, tax codes and regulations. Laws and regulations should not unduly discriminate between SOEs and their market competitors. SOEs' legal form should allow creditors to press their claims and to initiate insolvency procedures.

PHLPOST – and GOCCs more generally in the Philippines – enjoy strong protection against takeovers and are not subject to insolvency and bankruptcy rules.

As mentioned in Section 2.5, the acquisition of PHLPOST or a merger would require the enactment of an authorising law.⁵⁶ In addition, under PHLPOST's charter, and contrary to the generally applicable rules of the Corporation Code, potential private investors (PHLPOST is currently fully state-owned) are subject to two restrictions: 1) they may only acquire Class B shares (when the government decides to issue Class B shares); and 2) their (combined) shareholding may not exceed 55% of PHLPOST's total capital.⁵⁷ Even in the event of a private investor acquiring shares in PHLPOST, the government is still able to enforce the corporation's public-service mandate.⁵⁸

In case of financial distress, the government can intervene upon GCG recommendation. On a case-by-case basis, the Department of Finance can cover for the losses and would likely dispose of the assets.

The possibility of takeover and bankruptcy are essential for policing management in private-sector corporations. PHLPOST's special status may negatively influence its management and strategic decisions and therefore disrupt the level playing field (OECD, 2015, p. 12⁽⁴⁾).

The OECD has two recommendations.

1. Should the government decide to allow for private shareholders to invest in PHLPOST, the Corporation Code should equally apply to PHLPOST; the Postal Service Act should then be amended accordingly (OECD, 2015, pp. 47-48⁽⁴⁾).
2. PHLPOST should be subject to bankruptcy rules (OECD, 2015, pp. 47-48⁽⁴⁾). Any considerations with regard to PSO and its funding should be dealt with separately (see Section 4.2.1).

Public insurance scheme for vehicles

General principle

Transactions between the state and SOEs, and between SOEs, should take place on market consistent terms.

PHLPOST operates a fleet of approximately 380 vehicles, mainly employed for the delivery of small packages and mail. Under Republic Act No. 4136 (Land Transportation Act), PHLPOST-owned vehicles are subject to the same registration process and fees as those for privately owned commercial vehicles. Only the registration of "government automobiles" is free of charge,⁵⁹ but "motor vehicles owned by government corporations" – such as PHLPOST – are excluded from this definition.⁶⁰ Also, under Republic Act No. 8794, both privately owned vehicles and government owned vehicles are subject to the road-user tax.

For insurance coverage, GOCCs should insure their vehicles through the Government Service Insurance System (GSIS).⁶¹ Based on stakeholder input, GSIS premiums appear to be lower than the premiums for privately owned vehicles. In addition, GOCCs vehicles can be inspected at Land Transportation Office inspection centres and are subject to an inspection fee of approximately PHP 100, which is estimated to be approximately 70% lower than the fee for privately owned vehicles.

The impact on PHLPOST's cost structure is not negligible given the number of its vehicles, which although they may also be employed for public service purposes, are also used for PHLPOST's commercial business activities. As these advantages are not enjoyed by private entities, they may face higher costs for insurance and inspection fees compared to PHLPOST.

The OECD has one recommendation.

1. When calculating PHLPOST rates for its commercial activities, GSIS premiums and inspection fees should reflect market rates for GOCC-owned vehicles employed for commercial activities, such as PHLPOST's fleet. For such vehicles, PHLPOST should be given the opportunity to source insurance services outside the GSIS scheme - should the market allow for lower premiums and inspection fees.

Tax treatment

General principle

As a guiding principle, SOEs undertaking economic activities should not be exempt from the application of general laws, tax codes and regulations. Laws and regulations should not unduly discriminate between SOEs and their market competitors.

Philippine GOCCs, including PHLPOST, are not generally exempted from income tax.⁶² Nonetheless, PHLPOST's charter exempts it from the following taxes:

1. all taxes and duties on imported equipment, subject to a PHLPOST application to the Department of Finance
2. all taxes on financial obligations
3. capital gains tax
4. local government imposts and fees.⁶³

In principle, to maintain a level playing field, private competitors should be subject to equivalent tax treatment as GOCCs (OECD, 2015, p. 49^[41]). Nevertheless, the exemption from capital gains tax would appear justified due to the fact that GOCCs are required "to remit at least 50% of their annual net earnings as cash, stock or property dividends to the National Government".⁶⁴

As to local imposts and fees, PHLPOST indicated that some LGUs do not consider property taxes to fall under this exemption. Under Section 234 of the Local Government Code, real property taxes seem to apply to GOCCs to the extent that it is a "taxable person". Therefore, LGUs have requested that PHLPOST pay real property taxes computed from as early as 1992. In addition, Section 193 of the Local Government Code prescribes that all tax incentives or exemptions be withdrawn.

The OECD has one recommendation.

1. General exemptions from imported equipment duties, capital gains taxes and local government imposts and fees should be reviewed, and Section 14 of the Postal Service Act should be amended accordingly.

Given that PHLPOST's PSO are not directly funded (see Section 4.2.1), case-by-case exemptions may be granted if there is a link to PHLPOST's PSO-related investments or activities, for instance for costs incurred for establishing a presence in and delivering to non-profitable areas.

In addition, a study could be conducted as to how the capital gains tax exemptions compares to the level of remittances paid by PHLPOST.

5.2.6. Combination of commercial and non-commercial activities

Certain GOCCs may mix commercial and non-commercial activities that share costs, at least in part.

In principle, the Philippine state does not appear to subsidise GOCCs' non-commercial activities, which as a result are instead cross-subsidised by revenue generated through commercial activities. In such cases, GCG prescribes a policy framework for tasking GOCCs to undertake non-commercial programs, imposing – as one of its conditions – separate accounting and reporting obligations.⁶⁵ That said, it appears that PHLPOST's activities, including PSO, are not considered "non-commercial activities" for GCG's purposes and therefore are not subject to this GCG policy framework and system.

The OECD has no recommendation.

References

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- PHLPOST (2017), *PHLPOST 2017 Performance Report – 2017 Highlights of Accomplishments*, [3]
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Notes

¹ Section 23 of the Postal Service Act. Disputes with personnel are settled by the Department of Labor and Employment. Civil-service laws do not apply to top management directly appointed by the President.

² Although it is unclear whether the GOCC Governance Act of 2011 supersedes Section 9 of the Postal Service Act, it would appear that the Office of the President can adopt rules for the disposition of Class B shares and that these shares would be regulated under the Corporation Code.

³ From a legal perspective, a GCG Memorandum would be sufficient to “reorganise” PHLPOST; an amendment to the charter is not required. By contrast, as for other chartered GOCCs, a merger would require an authorising law; see *GCG Guidebook for Reorganization for GOCCs*.

⁴ GCG MO No. 2012-21.

⁵ PHLPOST is also working on a proposal to amend the Postal Service Act, allowing PHLPOST to engage into additional services in line with the international standards such as remittance services.

⁶ Sections 5(a) and (d) of the Postal Service Act.

⁷ Although Section 11 of the Postal Act allows PHLPOST to invest in government securities, such investments have hardly occurred. In the past, PHLPOST did fully own the Philippine Postal Savings Bank

(Postbank); this bank was acquired by Land Bank following Executive Order 44 (2017) and renamed Overseas Filipino Bank.

⁸ Section 8 of the Postal Service Act. The Postmaster General is appointed by the president as director, and thereafter appointed as CEO by the board of directors.

⁹ The main difference between these two services is the service commitment.

¹⁰ The CSC-COA-DBM Joint Circular No. 1-2017 (as well as CSC-COA-DBM Joint Circular 1-2018, an amendment of CSC-COA-DBM Joint Circular 1-2017) introduces a number of limitations and preconditions for government agencies, including GOCCs, to outsource jobs to other government entities, private firms or individuals, and non-government organisations. For example, outsourced activities are required not to be part of the regular function of the agency, and an “institutional contract of service” is required between a GOCC and a duly registered contractor or service provider.

¹¹ GCG MC No. 2017-02. PHLPOST’s 2017 Performance Scorecard and 2018 Performance Scorecard

¹² GCG MC No. 2017-02, Section 5.

¹³ Live sampling results generated by PHLPOST’s Service Regulations Department.

¹⁴ For instance, PHLPOST’s services were once referred to as “snail mail” (<https://edgedavao.net/the-economy/2018/01/23/philpost-regaining-publics-trust-exec/>).

¹⁵ See, for instance, a news report on a mail sorter arrested for allegedly stealing mail (www.philstar.com/metro/2000/11/06/107499/philpost-mail-sorter-nabbed-theft). Stakeholders also noted that PHLPOST does not effectively compete in large tenders due to lack of reputation and inefficiencies because its personnel – subject to civil-service rules – lacks motivation and skills. See also McKenzie (2012^[8]), p. 106.

¹⁶ Sections 5(a) and (d) of the Postal Service Act.

¹⁷ In compliance with UPU Manuals.

¹⁸ PHLPOST submitted that this obligation is limited to “committed areas” for express deliveries; these are areas where Express Mail Service (EMS) delivery standards apply.

¹⁹ This seems an issue common to GOCCs offering products and services below cost in the Philippines.

²⁰ Similarly, the express business is subsidising the non-express delivery of small packages.

²¹ Chapter 9, Section 42 of Executive Order No. 292 (Administrative Code).

²² However, PHLPOST has no ex officio directors.

²³ Section 18 of GOCC Governance Act of 2011.

²⁴ GCG MC No. 2012-05.

²⁵ Section 27 of GOCC Governance Act of 2011.

²⁶ Following NEDA’s guidelines. See, GCG MC No. 2015-01.

²⁷ In this regard, see OECD (2015^[4]), p. 37.

²⁸ In the Philippines, the franking privilege applies to the following bodies and individuals: President, Vice President, senators and members of the House of Representatives, Commission on Elections, former presidents, National Census and Statistics Office, general public in filing complaints against public offices, Supreme Court, Court of Appeals, Regional and Municipal Trial Courts, National Land Registration Authority, Register of Deeds, Office of Ombudsman, Public Attorney.

²⁹ Article 3, Section 1 of the 1987 Constitution.

³⁰ Reimbursements are usually processed every two years.

³¹ Section 531 of Local Government Code.

³² See also, OECD (2015^[4]), p. 47: “both over compensation and under compensation shall be avoided”.

³³ Issues related to the franking privilege were also raised in 2008 in Senate Resolution No. 799 by Senator M.D. Santiago, who reported a postmaster’s statement claiming that PHLPOST “has been losing about PHP 200 million a year for the franking privileges given to the executive and legislative department”.

³⁴ Section 105.2(c) of Amended Memorandum of Agreement.

³⁵ Section 106.1 of Amended Memorandum of Agreement.

³⁶ Section 109.1 of Amended Memorandum of Agreement.

³⁷ Section 111.1.3 of Amended Memorandum of Agreement.

³⁸ Meaning that the provisions will be made to apply only where there is an insufficiency in the applicable rule.

³⁹ Sections 5 and 6 of Postal Service Act.

⁴⁰ Section 4 of the Postal Service Act, prior to regulatory competences being transferred to DICT-PRD.

⁴¹ The last increase was approved in 2014, which means – according to PHLPOST – that the current minimum rates do not reflect the increased costs. A request to amend minimum rates can be filed either by PHLPOST or by private SPDS providers.

⁴² Section 2 of the Republic Act No. 9184 (Government Procurement Reform Act), which promotes the good governance of all the government branches, including GOCCs, and 2016 Implementing Rules and Regulations of Republic Act No. 9184.

⁴³ Article 23(5) of 2016 Implementing Rules and Regulations of Republic Act No. 9184.

⁴⁴ Private companies have to register with the Philippine Government Electronic Procurement System (PhilGEPS) to pre-qualify for public tenders.

⁴⁵ Section 53.5 of the 2016 Implementing Rules and Regulations of the Government Procurement Reform Act (“alternative methods”).

⁴⁶ Section 66 and ff of the Administrative Code of 1987 and Article 30 of GCG MC No. 2012-06.

⁴⁷ Title III, Chapter 1 of the Administrative Code of 1987.

⁴⁸ This is the result of Section 12 of the Local Government Code stating that local authorities “shall endeavour to establish a government center” where – among other services – GOCCs may be located.

⁴⁹ It should be noted, however, that – even under such terms – PHLPOST does not always agree to establish a branch, for instance if it considers the estimated volumes will be too low.

⁵⁰ Section 25 of GOCC Governance Act of 2011.

⁵¹ Noted as “Subsidy Income from National Govt” on page 2 of PHLPOST’s 2017 Financial Statements..

⁵² Pursuant to Section 13 of the Postal Service Act, PHLPOST’s budget is not subject to congressional approval, except when PHLPOST submits a request for a subsidy or a guarantee of its liability from the National Treasury.

⁵³ Section 12(f) of the Postal Service Act: “issuance of bonds or long-term notes shall be with prior approval of or in accordance with the rules issued by the National Treasurer.”

⁵⁴ Section 12(b) of the Postal Service Act: “foreign indebtedness can only be contracted with the concurrence of the Department of Finance, or under such terms and conditions established by the Central Bank.”

⁵⁵ Commission Notice on the application of Articles 87 and 88 of the EC Treaty to State aid in the form of guarantees, OJ C 155, 20.6.2008, p. 10-22.

⁵⁶ GCG Guidelines Covering the Merger or Abolition of GOCCs, GCG MC 2015-03, dated 8 April 2015.

⁵⁷ Section 9 of the Postal Service Act.

⁵⁸ For instance, through a “golden share” for specific matters; see OECD (2015_[4]), p. 52.

⁵⁹ Section 8(h) of Land Transportation Act.

⁶⁰ Section 7(m) of Land Transportation Act.

⁶¹ Section 5 of Republic Act No. 656 (as amended by Presidential Decree No. 245).

⁶² Section 1 of Republic Act No. 9337, amending Section 27(c) of National Internal Revenue Code of 1997.

⁶³ Section 14 of the Postal Service Act.

⁶⁴ Section 3 of the Republic Act No. 7656.

⁶⁵ Article 29 of GCG MC No. 2012- 06.

Annex A. List of reviewed legislation

Commonwealth Act No. 146 (Public Service Act) (1936)

Republic Act No. 4136 (Land Transportation Act) (1964)

Constitution of the Republic of the Philippines (1987)

Executive Order No. 292 – Administrative Code (1987)

Republic Act No. 7160 (Local Government Code) (1991)

Republic Act No. 7354 (Postal Service Act) (1992)

Supreme Court G.R. No. 105371 (Franking Privilege) (1993)

Republic Act No. 8794 (Motor Vehicle User's Charge Law) (2000)

Republic Act No. 9184 (Government Procurement Act) (2002)

Republic Act No. 9184 – Implementing Rules and Regulations (2002)

Republic Act No. 9337 – Amendments to Internal Revenue Code (Section 1(c)) (2005)

Senate Resolution directing inquiry into franking privilege (2008)

Executive Order No. 7 by the President of the Philippines (2010)

Executive Order No. 47 by the President of the Philippines (2011)

Executive Order No. 24 by the President of the Philippines (2011)

Office of the Court Administrator Circular No. 64-2011

Republic Act No. 10149 (GOCC Governance Act) (2011)

Executive Order No. 80 by the President of the Philippines (2012)

GCG Memorandum Circular No. 2012-04 (4th Issue) – Nomination and Shortlisting

GCG Memorandum Circular No. 2012-05 – Fit and Proper Rule

GCG Memorandum Circular No. 2012-06 – Ownership and Operations Manual

GCG Memorandum Circular No. 2012-07 – Code of Corp Governance

GCG Memorandum Circular No. 2012-09 (3rd Issue) – The Chief Executive Officer (CEO)

GCG Memorandum Circular No. 2012-10 (3rd Issue) – Directors' & Officers' Liability Insurance (DOLI)

GCG Memorandum Order No. 2012-21 – Rationalization of Philippine Postal Corporation

GCG Memorandum Order No. 2012-22 – Reclassifying the PHILPOST Leasing and Financing Corporation (PLFC) as Dissolved/ Liquidated/ Inactive

GCG Memorandum Circular No. 2013-04 – Establishment of the GCG Multi-Sector Governance Council

GCG Memorandum Circular No. 2013-05 (Re-Issued) – Interim Performance-based Bonus

GCG Memorandum Circular No. 2013-06 (Re-Issued) – Performance Incentive

GCG Memorandum of Agreement with Ombudsman (2013)

Philippine Postal Corporation – Schedule of Government Subsidy (2013)

GCG Memorandum Circular No. 2014-03 – Evaluation of Directors

GCG Memorandum of Agreement with Security Exchange Commission (2014)

GCG Memorandum Circular No. 2015-01 – Guidelines for the Creation of GOCCs and Related Corporations

GCG Memorandum Circular No. 2015-03 – Guidelines Covering the Merger or Abolition/Dissolution of GOCCs

GCG Memorandum Circular No. 2015-04 (Re-Issued) – Reorganization, Rationalization and Personnel Planning in the GOCC Sector

GCG Memorandum Circular No. 2015-07 – Corporate Governance Scorecard (CGS) for GOCCs

GCG Memorandum Order No. 2015-08 – Reorganization of the Philippine Postal Savings Bank, Inc.

Executive Order No. 203 by the President of the Philippines (2016)

GCG Memorandum Circular No. 2016-01 – Compensation Framework for Members of the GOCC Governing Boards

GCG Memorandum Circular No. 2016-02 – Revised Whistleblowing Policy for the GOCC Sector

Memorandum of Agreement between Bureau of Customs and PHLPOST (2016)

Philippine Postal Corporation 2016 Performance Scorecard (2016)

Republic Act No. 10844 (DICT Act) (2016)

Republic Act No. 10844 – Implementing Rules and Regulations (2016)

Supreme Court G.R. No. 212530 (Bloomberg vs. Bureau of Internal Revenue) (2016)

CSC-COA-DBM Joint Circular 1 – Contract of Service Workers (2017)

Executive Order 44 by the President of the Philippines (2017)

GCG Memorandum Circular No. 2017-02 - Interim PES for the GOCC Sector

GCG Memorandum Circular No. 2017-03 - Implementing Rules and Regulations of Executive Order No. 36 s.2017

Philippine Postal Corporation 2017 Performance Scorecard (2017)

Republic Act No. 11032 (Ease of Doing Business Act) (2017)

CSC-COA-DBM Joint Circular 1 – Contract of Service Workers (2018)

GCG Memorandum Circular No. 2018-02 – Revocation of GCG Memorandum Circular No. 2013-03 (Re-Issued) – Coordination and Alignment of Major Development Projects of the GOCC Sector

Senate Bill No. 1754 (Amendment to “public service”) (2018)

Republic Act No. 11232 (Revised Corporation Code) (2019)

Other related documents

GCG Guidebook for Reorganization of GOCCs

GCG Citizen’s Charter:

- Request for Reorganization of a GOCC
- Request for Merger of a GOCC
- Request for Privatization of a GOCC
- Request for Abolition of a GOCC.

OECD COMPETITIVE NEUTRALITY REVIEWS: SMALL-PACKAGE DELIVERY SERVICES IN THE PHILIPPINES

Efficient logistics can play a significant role in increasing a country's economic development by facilitating international trade and improving its competitiveness. This report focuses on small-package delivery services in the logistics sector and identifies the advantages or disadvantages of state-owned enterprises in this sector when competing with private companies.

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