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Tax bulletin



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PHILIPPINE TAX FIRM
OF THE YEAR
AND
TRANSACTION TAX TEAM
OF THE YEAR

Highlights

BIR Rulings

- ▶ A BOI-registered developer of a low-cost mass housing project is exempt from income tax and creditable withholding tax (CWT) on revenues derived from the registered activity. The exemption shall not extend to sales of units with selling price exceeding P3,000,000. In the computation of ITH, interest income from in-house financing shall not be considered as revenues generated from the registered activity.

A BOI-registered developer of a low-cost mass housing project is subject to VAT and DST on its sale of housing units. However, the sale of a residential lot valued at P1,919,500 and below, or a house and lot, and other residential dwellings, valued at P3,199,200 and below, is VAT exempt. **(Page 3)**

- ▶ Under the RP-Netherlands Tax Treaty, dividends paid by a domestic corporation to a resident of the Netherlands are subject to the 10% preferential tax rate, if the recipient is a company whose capital is wholly or partially divided into shares and which holds directly at least 10% of the capital of the Philippine company paying the dividends. **(Page 4)**

BIR Issuances

- ▶ Revenue Memorandum Circular (RMC) No. 52-2013 clarifies the validity period of unused/unissued principal and supplementary receipts/invoices printed prior to January 18, 2013. **(Page 4)**
- ▶ RMC No. 57-2013 circularizes BIR Ruling No. 123-2013 dated March 25, 2013 on the recovery of unutilized creditable input taxes attributable to VAT zero-rated sales, and enjoins BIR employees engaged in the audit/review of audit cases to disallow unutilized creditable input taxes attributable to VAT zero-rated sales that are claimed as a deduction for income tax purposes. **(Page 5)**

BSP Issuances

- ▶ Circular No. 805 requires BSP-supervised financial institutions to provide priority lanes to senior citizens, and amends Subsection X160.11 of the Manual of Regulations for Banks (MORB) and Subsection 4160Q.11, Subsection 4657S.10, Section 4658P and Section 4158N of the Manual of Regulations for Non-Bank Financial Institutions (MORNBFI) for this purpose. **(Page 6)**
- ▶ Circular No. 806 provides for the establishment of two separate rediscounting windows: Rediscounting Window I (RW I) for universal and commercial banks, and Rediscounting Window II (RW II) for thrift, rural and cooperative banks, and amends Section X269 and Subsections X.268.2, X.268.3, X.269.5, X269.6 and X.269.10 of the MORB for this purpose. **(Page 7)**
- ▶ Circular No. 807 prescribes changes in the exporter's dollar and yen rediscount facility (EDYRF), and amends Section X269 of the MORB for this purpose. **(Page 8)**
- ▶ Circular No. 808 prescribes guidelines on Information Technology Risk Management for all banks and other BSP-supervised institutions, and amends Sections X176 and X705 of the MORB for this purpose. **(Page 8)**
- ▶ Circular No. 809 amends the MORB to implement Republic Act (RA) No. 10574, otherwise known as "An Act Allowing the Infusion of Foreign Equity in the Capital of Rural Banks, amending The Rural Banks Act of 1992." **(Page 10)**

- ▶ Circular No. 810 amends the guidelines governing the issuance of long-term negotiable certificates of time deposits (LTNCTD). (Page 11)

Court Decisions

- ▶ A taxpayer who is exempt from both direct and indirect taxes can file a claim for refund of excise taxes which were passed on to it by its supplier. (Page 12)
- ▶ A company that operates, maintains, and manages a power plant for the conversion of fuel into electricity, which is in turn sold to customers, is classified as a manufacturer/producer for local business tax purposes.

Attorney's fees may be awarded when the city's act or omission compelled the taxpayer to litigate or to incur expenses to protect his interest. (Page 13)

- ▶ In a criminal case for willful and felonious failure to pay taxes, the prosecution must establish the guilt of the accused beyond reasonable doubt, by proving that the taxpayer is legally required to pay the assessed tax, and that the accused willfully and feloniously failed to pay the assessment at the time legally required to do so. (Page 14)
- ▶ The failure to strictly comply with the requirement under Revenue Memorandum Order (RMO) No. 1-2000 to file an application for tax treaty relief (TTRA) 15 days prior to the avilment of the provisions of a tax treaty, should not deprive a taxpayer of the benefit of a tax treaty.

The Supreme Court's Minute Resolution in the Mirant case is not a binding precedent. (Page 16)

BIR Rulings

BIR Ruling No. 317-2013 dated August 12, 2013

A BOI-registered developer of a low-cost mass housing project is exempt from income tax and CWT on revenues derived from the registered activity. The exemption shall not extend to sales of units with selling price exceeding P3,000,000. In the computation of ITH, interest income from in-house financing shall not be considered as revenues generated from the registered activity.

A BOI-registered developer of a low-cost mass housing project is subject to VAT and DST on its sale of housing units. However, the sale of a residential lot valued at P1,919,500 and below, or a house and lot, and other residential dwellings, valued at P3,199,200 and below, is VAT exempt.

Facts:

A Co., a domestic corporation engaged in the real estate business, is registered with the Board of Investments (BOI) as a new developer of a low-cost mass housing project on a non-pioneer status, and was granted a 4-year Income Tax Holiday (ITH) on revenues generated from its low-cost mass housing project.

Issues:

1. Are sales from the registered project exempt from CWT, VAT and DST?
2. Is A Co.'s entitlement to ITH automatic?
3. Is A Co. constituted as withholding agent for its income payments subject to withholding tax?
4. Is A Co. subject to any other administrative requirement?

Ruling:

1. Sales from the registered project are exempt from CWT. Under Section 2.57.5(B)(2) of Revenue Regulations (RR) No. 2-98 CWT shall not apply to income payments to persons enjoying exemption from income tax, such as BOI-registered enterprises enjoying ITH. However, the exemption covers only the revenues generated from the registered activity, such as low-cost mass housing, and shall not extend to sales of units with selling price exceeding P3,000,000. In the computation of ITH, interest income from in-house financing shall not be considered as revenues generated from the registered activity.

A BOI-registered enterprise enjoys no tax exemption/privileges other than those granted under Executive Order (EO) No. 226 and the terms and conditions of its BOI registration. Thus, A Co. will remain subject to VAT and DST on its sales of house and lot units pursuant to Sections 106(A)(1)(a) and 196 of the Tax Code, except that the sale of a residential lot valued at P1,919,500 and below, or a house and lot and other residential dwellings valued at P3,199,200 and below, is VAT exempt.

2. No. Entitlement to ITH is not automatic. A Co. still has to comply with the Specific Terms and Conditions of its BOI registration.
3. Yes. A Co. shall be constituted as a withholding agent by the government if it acts as employer and any of its employees receives compensation income subject to WT on compensation, or if it makes payments to individuals or corporations subject to WT at source pursuant to RR No. 2-98, as amended.
4. Yes. A Co. is required to file on or before the 15th day of the 4th month following the close of its accounting period a Profit and Loss Statement and Balance Sheet with Annual Information Return under oath, stating its gross income and expenses incurred during the taxable year. Furthermore, A Co.'s books of accounts and other pertinent records shall be subject to periodic examination by the BIR for the purpose of ascertaining its compliance with the conditions for tax exemption or incentives and its tax liabilities, if any.

BIR Ruling No. ITAD 212-13 dated July 31, 2013

Under the RP-Netherlands Tax Treaty, dividends paid by a domestic corporation to a resident of the Netherlands are subject to the 10% preferential tax rate, if the recipient is a company whose capital is wholly or partially divided into shares and which holds directly at least 10% of the capital of the Philippine company paying the dividends.

Facts:

A Co., a nonresident foreign corporation based in the Netherlands, owns 100% of the total outstanding shares in B Co., a domestic corporation. B Co. declared cash dividends in favor of A Co.

Issue:

Are the dividends paid by B Co. to A Co. entitled to the 10% preferential tax rate under the RP-Netherlands Tax Treaty?

Ruling:

Yes. Under the RP-Netherlands Tax Treaty, dividends paid by a domestic corporation to a resident of the Netherlands are subject to the preferential tax rate of 10% of the gross amount of dividends, if the recipient is a company whose capital is wholly or partially divided into shares and holds directly at least 10% of the capital of the Philippine company paying the dividends.

BIR Issuances

RMC No. 52-2013 clarifies the validity period of unused/unissued principal and supplementary receipts/invoices printed prior to January 18, 2013.

Revenue Memorandum Circular No. 52-2013 dated August 13, 2013

- ▶ All principal and supplementary receipts or invoices with authority to print (ATP) dated prior to January 1, 2011 shall no longer be valid as of August 31, 2013, pursuant to RR No. 18-2012 and RMC No. 44-2013.

- ▶ Issuance of said receipts/invoices starting August 31, 2013 shall be a violation of Section 264 of the Tax Code and will have the following effects:
 1. No receipt/invoice shall be considered to have been issued.
 2. No deduction from gross income shall be allowed using these receipts/invoices, as they are not valid proof of substantiation.
 3. No input tax may be claimed by VAT-registered persons using these receipts/invoices.
- ▶ All principal and supplementary receipts/invoices with ATP dated January 1, 2011 to January 17, 2013 may be used until October 31, 2013 provided that a new ATP was issued on or before August 30, 2013.
- ▶ A new ATP filed after April 30, 2013 is considered filed out of time and subject to penalty of P1,000.00.
- ▶ In all principal and supplementary receipts/invoices which can be used until October 31, 2013, the phrase "valid until October 31, 2013 only" shall be stamped prominently on the face of the receipts/invoices (original and duplicate copies).
- ▶ A certified true copy of the ATP should be attached to any application for tax clearance and failure to submit the same shall be a ground for the non-issuance of the tax clearance for whatever purposes.

RMC No. 57-2013 circularizes BIR Ruling No. 123-2013 dated March 25, 2013 on the recovery of unutilized creditable input taxes attributable to VAT zero-rated sales, and instructs BIR employees engaged in the audit/review of audit cases to disallow unutilized creditable input taxes attributable to VAT zero-rated sales that are claimed as a deduction for income tax purposes.

Revenue Memorandum Circular No. 57-2013 dated August 23, 2013

- ▶ In BIR Ruling No. 123-2013 dated March 25, 2013, the Commissioner ruled:

"In reply, please be informed that Section 110(B), in relation to Section 112(A) of the 1997 Tax Code, as amended, provides for the remedy of a taxpayer to recover the unapplied accumulated input VAT arising from zero-rated transactions, viz:

'110. Tax Credits. -

xxx xxx xxx

'B) Excess Output or Input Tax. - If at the end of any taxable quarter the output tax exceeds the input tax, the excess shall be paid by the VAT-registered person. If the input tax exceeds the output tax, the excess shall be carried over to the succeeding quarter or quarters. **Any input tax attributable to the purchase of capital goods or to zero-rated sales by a VAT-registered person may at his option be refunded or credited against other internal revenue taxes, subject to the provisions of Section 112.** (Underscoring supplied)

xxx xxx xxx'

"In addition thereto, Section 112(A) of the same Code states:

'(A) Zero-Rated or Effectively Zero-Rated Sales. - Any VAT-registered person, whose sales are zero-rated or effectively zero-rated may, within two (2) years after the close of the taxable quarter when the sales were made, apply for the issuance of a tax credit certificate or refund of creditable input tax due or paid attributable to such sales, except transitional input tax, to the extent that such input tax has not been applied against output tax: xxx xxx xxx (Underscoring supplied)'

"It is noted, based on the above-cited provisions, that unutilized creditable input taxes attributable to zero-rated sales can only be recovered through the application for refund or tax credit. Nowhere in the Tax Code can we find a specific provision expressly providing for another mode of recovering unapplied input taxes, particularly your proposition that unapplied input taxes may be treated outright as deductible expense for income tax purposes. Thus, your proposition, that accumulated and unapplied input value-added tax (VAT) arising from Cekas' purchase of goods and services after the expiration of the two (2) year prescriptive period may be expensed outright, is hereby denied for lack of legal basis.

"It is a governing principle in taxation that tax exemptions must be construed in *strictissimi juris* against the taxpayer and liberally in favor of the taxing authority. The basic principle in the construction of laws granting tax exemptions has been very stable. He who claims an exemption from his share of the common burden of taxation must justify his claim by showing that the Legislature intended to exempt him by words too plain to be beyond doubt or mistake (*City of Iloilo, et.al. vs. Smart Communications, Inc. G.R. No. 167260*, dated February 27, 2009). And since a deduction for income tax purposes partakes the nature of a tax exemption, then it must also be strictly construed (*CIR vs. Isabela Cultural Corporation, G.R. No. 172231 dated February 12, 2007*)."

- ▶ All other issuances inconsistent herewith are hereby repealed or modified accordingly.
- ▶ All revenue officials and employees are encouraged to give this Circular as wide publicity as possible. Accordingly, all employees engaged in the audit and review of audit cases are hereby instructed to disallow unutilized creditable input taxes attributable to VAT zero-rated sales that is claimed as a deduction for income tax purposes.
- ▶ This Circular shall take effect immediately.

[Editor's Note: BIR Ruling No. 123-13 was featured in our June 2013 Tax Bulletin.]

BSP Issuances

Circular No. 805 requires BSP-supervised financial institutions to provide priority lanes to senior citizens, and amends Subsection X160.11 of the Manual of Regulations for Banks (MORB) and Subsection 4160Q.11, Subsection 4657S.10, Section 4658P and Section 4158N of the Manual of Regulations for Non-Bank Financial Institutions (MORNBFI) for this purpose.

BSP Circular No. 805 dated August 8, 2013

- ▶ Senior citizens shall be provided with express lanes in all banking and quasi-banking establishments, non-stock savings and loan associations (NSSLAs), pawnshops and non-bank financial institutions (NBFIs).
- ▶ If the provision of express lanes is logistically impossible in any particular branch of office of any bank, quasi-bank, NSSLA, pawnshop and NBF, said branch or office shall ensure that senior citizens are accorded priority service.

- ▶ The provision of express lanes and/or priority service shall be made known to the general public through a clearly written notice prominently displayed in the transaction counters.
- ▶ Circular No. 805 shall take effect 15 days following its publication either in the Official Gazette or in a newspaper of general circulation.

[Editor's Note: Circular No. 805 was published in the Manila Bulletin on August 17, 2013.]

Circular No. 806 provides for the establishment of two separate rediscounting windows: Rediscounting Window I (RW I) for universal and commercial banks, and Rediscounting Window II (RW II) for thrift, rural and cooperative banks, and amends Section X269 and Subsections X.268.2, X.268.3, X.269.5, X269.6 and X.269.10 of the MORB for this purpose.

BSP Circular No. 806 dated August 15, 2013

- ▶ Banks applying for rediscounting line shall submit their application to the Department of Loans and Credits (DLC), BSP Manila. Submission of application to the Regional Loans and Credit Division (RLCD) of BSP Regional Offices is no longer allowed.
- ▶ Marketable debt instruments issued by the National Government and all its instrumentalities, including US\$ denominated bonds or ROPs are now accepted as security for credit instruments acquired under commercial and other credits. The collateral value shall equal or exceed the outstanding balance of the Promissory Notes (PN).
- ▶ The maturities of BSP rediscounts are revised as follows:

Type of Credit	Maturity Date	
	RW I	RW II
Commercial Credits (1) Export packing (2) Trading (3) Transport (4) Quedan (5) Export Bills (EB)	180 days from date of rediscount but shall not go beyond the maturity date of the credit instrument	180 days from date of rediscount but shall not go beyond the maturity date of the credit instrument
At sight	15 days from date of purchase	15 days from date of purchase
Usance EB	Term of draft but not to exceed 60 days from shipment date	Term of draft but not to exceed 60 days from shipment date
Production Credits	180 days from date of rediscount but shall not go beyond the maturity date of the PN. Renewable, not to exceed 180 days.	360 days from date of rediscount but shall not go beyond the maturity date of the PN.
Other Credits	180 days from date of rediscount but shall not go beyond the maturity date of the PN. Renewable depending on the type of credit.	360 days from date of rediscount but shall not go beyond the maturity date of the PN. Renewable depending on the type of credit.

- ▶ The rediscount/lending rates for peso rediscounts are now as follows:

	RW I	RW II
Interest Rate	BSP 1-month repurchase (R/P) rate plus term premium	BSP overnight reverse repurchase (O/N RRP) rate plus term premium
30 days	BSP 1-month R/P rate	
90 days	BSP 1-month R/P rate + 0.0625	BSP O/N RRP rate
180 days	BSP 1-month R/P rate + 0.1250	BSP O/N RRP rate + 0.0625
360 days	n/a	BSP O/N RRP rate + 0.1250

- ▶ Circular No. 806 shall take effect on November 15, 2013. From the effectivity of the Circular, thrift banks are given a sunset period of five years (until November 15, 2018) to access RW II, while rural and cooperative banks are given 10 years (until November 15, 2023). By November 15, 2023, all banks shall access only RW I.

[Editor's Note: Circular No. 806 was published in Manila Standard Today on August 28, 2013.]

Circular No. 807 prescribes changes in the EDYRF, and amends Section X269 of the MORB for this purpose.

BSP Circular No. 807 dated August 15, 2013

- ▶ Dollar-denominated trust receipts covering importation of goods and raw material are also considered eligible papers for rediscounting under the exporter's dollar and yen rediscount facility (EDYRF).
- ▶ Dollar-term loans to finance capital expenditures by exporters are also considered eligible papers for rediscounting under the EDYRF provided they are booked in the regular banking units.
- ▶ The rediscount rates for dollar and yen loans are as follows:

Term	Premium
1-90 days	90-day LIBOR + 200 bps
91-180 days	90-day LIBOR + 200 bps + 6.25 bps
181-360 days	90-day LIBOR + 200 bps + 12.50 bps

- ▶ The foreign exchange (FX) rate at the time of loan repayment shall not be lower than the FX rate at the time of the loan availment, and any FX loss arising from default or repayment shall be for the account of the borrower and not for the BSP.
- ▶ Circular No. 807 shall take effect on November 15, 2013.

[Editor's Note: Circular No. 807 was published in The Business Mirror on August 28, 2013.]

Circular No. 808 prescribes guidelines on Information Technology Risk Management for all banks and other BSIs, and amends Sections X176 and X705 of the MORB for this purpose.

BSP Circular No. 808 dated August 22, 2013

- ▶ The BSP shall risk profile all BSP-supervised institutions (BSIs) and classify them as either "complex" or "simple", depending on their dependence on technology. By default, thrift, rural and cooperative banks are classified as "simple", while universal and commercial banks are classified as "complex". BSIs may be reclassified based on the assessment of their Information Technology (IT) profile report.

- ▶ BSIs are required to establish a robust Information Technology Risk Management (ITRM) system covering four key components:
 1. IT Governance - leadership and organizational structures and processes covering the following:
 - a. Oversight and Organization of IT Functions
 - b. IT Policies, Procedures and Standards
 - c. IT Audit
 - d. Staff Competence and Training
 - e. Management Information Systems (MIS)
 - f. IT Risk Management Function
 2. Risk Identification and Assessment
 - a. BSIs should maintain a risk assessment process that drives response selection and controls implementation.
 - b. Periodic risk assessment process should be done at the enterprise-wide level and an effective monitoring program for the risk mitigation activities should be manifested through mitigation or corrective action plans, assignment of responsibilities and accountability and management reporting.
 3. IT Controls Implementation - Management should implement satisfactory control practices that address the following as part of its overall IT risk mitigation strategy:
 - a. Information security
 - b. Project Management/Development and Acquisition and Change Management
 - c. IT Operations
 - d. IT Outsourcing/Vendor Management Program
 - e. Electronic Products and Services
 4. Risk Measurement and Monitoring
 - a. BSI Management should monitor IT risks and the effectiveness of established controls through periodic measurement of IT activities based on internally established standards and industry benchmarks.
 - b. The scope and frequency will depend on the complexity of the BSI's IT risk profile and should cover, among others, the following:
 - ▶ Performance vis-à-vis Approved IT Strategic Plan
 - ▶ Performance Benchmarks/Service Levels
 - ▶ Quality Assurance/Quality Control
 - ▶ Policy Compliance
 - ▶ External Assessment Program
- ▶ BSIs are required to submit the following reports to BSP:
 1. Annual IT Profile, electronically to the BSP Supervisory Data Center (SDC) within 25 days from the end of reference year
 2. Report on breach in information security

3. Notification letter to the Core Information Technology Specialist Group (CITSG) of the BSP of disruption of IT services/operations that resulted to the activation of disaster recovery and business continuity plan immediately upon activation of the plan.

- ▶ Violations shall be subject to the monetary and non-monetary sanctions under Section 37 of The New Central Bank Act. Additional sanctions may be imposed when BSI's ITRMS exhibit deficient IT environment that may impair the future viability of the entity.
- ▶ Circular No. 808 shall take effect 15 days following its publication either in the Official Gazette or in a newspaper of general circulation.

[Editor's Note: Circular No. 808 was published in The Philippine Star on August 30, 2013.]

Circular No. 809 amends the MORB to implement Republic Act (RA) No. 10574, otherwise known as "An Act Allowing the Infusion of Foreign Equity in the Capital of Rural Banks, amending The Rural Banks Act of 1992."

BSP Circular No. 809 dated August 23, 2013

- ▶ Limits of stockholdings in a single rural bank:
 1. Foreign individuals and non-bank corporations:
 - Individual - 60% of the voting stock
 - Aggregate - 60% of the voting stock
 2. Qualified foreign banks:
 - Individual limit - 60% of the voting stock
 - Aggregate limit - 60% of the voting stock
 3. Filipino individual and domestic non-bank corporation:
 - Individual limit - 60% of the voting stock
 - Aggregate limit - no ceiling
 4. Individual and corporation/s which is/are wholly-owned, or with majority of the voting stock owned by him: Combined 60% of the voting stock
 5. Family groups and related interests: Individual limit - 60% of the voting stock
- ▶ In case of rural banks, a corporate stockholder shall be deemed Filipino-owned if it is organized under the laws of the Philippines and at least 60% of its capital is owned by Filipino citizens.
- ▶ The Land Bank of the Philippines (LBP), Development Bank of the Philippines (DBP) or any government-owned or controlled bank or financial institution, on representation of private shareholders, shall subscribe to the capital stock of any rural bank, which shall be paid in full at the time of subscription, in an amount equal to the fully paid subscribed and unimpaired capital of the private stockholders, or such amount as may be prescribed by the Monetary Board.
- ▶ Individuals, banks and non-bank corporations may, subject to applicable ownership ceilings, own voting shares in such number of rural banks as may be authorized by the Monetary Board.
- ▶ Shares in a rural bank held by LBP, DBP or any government-owned or controlled bank or financial institution may be sold at any time at adjusted book value.

- ▶ The guidelines in selecting the foreign bank which will be allowed to invest in majority of the voting stock of an existing domestic bank, or to establish a subsidiary or branch in the Philippines under Subsection X105.3, shall apply to foreign banks seeking to own, acquire or purchase up to 60% of the voting stock in a rural bank.
- ▶ Government shares held on or after the effectivity of the implementing rules and regulations of RA No. 10574 shall share in dividend distributions from the date of issuance in an amount based on the lending benchmark approved by the BSP, plus the prevailing non-prime spread of the government financial institution. The rural bank and the government-owned or controlled bank are not precluded from entering into an agreement providing for other rates.
- ▶ In case of rural banks, at least one independent director shall be elected. Rural banks with complex business model shall have at least 20% but not less than two independent directors.
- ▶ Rural banks not qualified to acquire or hold lands in the Philippines shall be allowed to bid and take part in foreclosure sales of real property mortgaged to them, and to take possession thereof for a period not exceeding five years. Title to the property shall not be transferred to such rural bank. In case such rural bank fails to transfer the property within the five year period, it shall be penalized at ½ of 1% per annum of the price at which the property was foreclosed until transferred to a qualified Philippine national.
- ▶ Circular No. 809 shall take effect 15 days following its publication either in the Official Gazette or in a newspaper of general circulation.

[Editor's Note: Circular No. 809 was published in The Manila Times and Malaya on August 29, 2013.]

Circular No. 810 amends the guidelines governing the issuance of LTNCTD.

BSP Circular No. 810 dated August 30, 2013

- ▶ The following additional requirements shall be submitted within 10 calendar days after the issuance of the initial offering/tranche:
 1. Written waiver of the secrecy of deposits on said long-term negotiable certificates of time deposits (LTNCTD) by the issuing bank, its subsidiaries, affiliates and wholly or majority-owned or -controlled entities of such subsidiaries and affiliates;
 2. Information disclosure and the terms and conditions of the LTNCTD issuance;
 3. Promotional materials; and
 4. Specimen of the proposed registry confirmation and purchase advice from each selling agent/market maker which will evidence sale of the LTNCTD.
- ▶ The issuing bank may change its registry bank, underwriter/arranger, selling agent and/or market maker, provided it notifies the appropriate department of the SES in writing within 10 calendar days from the date of such change.
- ▶ Circular No. 810 shall take effect 15 days following its publication either in the Official Gazette or in a newspaper of general circulation.

[Editor's Note: Circular No. 810 was published in the Business Mirror on September 6, 2013.]

Court Decisions

Philippine Air Lines vs. Commissioner of Internal Revenue

Supreme Court (Second Division) G.R. No. 198759 promulgated July 1, 2013

A taxpayer who is exempt from both direct and indirect taxes can file a claim for refund of excise taxes which were passed on to it by its supplier.

Facts:

Caltex sold imported Jet A-1 fuel to Philippine Air Lines (PAL) for the latter's domestic operations. Caltex issued to PAL an Aviation Billing Invoice that included the related excise taxes on the sale. In a certification, Caltex confirmed that it paid excise taxes on the imported petroleum products and that it passed-on these excise taxes to PAL. Caltex also certified that it did not file with the BIR any claim for refund of the said excise taxes.

PAL filed a claim for refund of the excise taxes passed on to it by Caltex, on the ground that it is exempt from certain taxes on its purchase or importation of aviation gas, fuel, and oil, including those which are passed-on to it by the seller or importer. Due to the CIR's inaction, PAL filed a Petition for Review with the Court of Tax Appeals (CTA). The CTA denied the claim on the ground that only Caltex, the statutory taxpayer of the excise taxes, had the personality to file the refund claim of the excise taxes paid.

The CTA ruled that indirect taxes remained to be the direct liability of Caltex, the statutory taxpayer, and that although the tax burden may have been shifted to PAL, the amount should form part of the purchase price which PAL had to pay to obtain the goods. Moreover, the CTA ruled that PAL's exemption privileges "*on its purchase of domestic petroleum products for use in its domestic operations*" had already been withdrawn by Letter of Instruction (LOI) No. 1483.

Issues:

1. Does PAL have the legal personality to file a claim for refund of the passed-on excise taxes?
2. Is the sale of imported aviation fuel by Caltex to PAL covered by the withdrawal of PAL's tax exemption privileges in LOI No. 1483?

Ruling:

1. Yes, PAL can file a claim for refund of the passed-on excise taxes.

As a rule, indirect taxes are those which are demanded in the first instance from one person with the expectation that he can shift the economic burden to someone else. The statutory taxpayer can transfer to its customers the value of the excise taxes it paid, or would be liable to pay, to the government by treating it as part of the cost of goods and tacking it on to the selling price. The manufacturer/producer, or importer remains to be the statutory taxpayer of the excise tax, which has the legal personality to file the claim for refund. However, this does not apply to instances where the law clearly grants the party to which the economic burden of the tax is shifted an exemption from both direct and indirect taxes. In such instance, the latter must be allowed to claim a tax refund even if it is not considered the statutory taxpayer.

The propriety of a tax refund claim depends on the kind of exemption which forms its basis. If the law confers an exemption from both direct or indirect taxes, a claimant is entitled to a tax refund even if it only bears the economic

burden of the applicable tax. On the other hand, if the exemption conferred only applies to direct taxes, then the statutory taxpayer is regarded as the proper party to file the refund claim.

PAL's franchise grants it an exemption from both direct and indirect taxes on its purchase of petroleum products. Thus, PAL's payment of either the basic corporate income tax or franchise tax, whichever is lower, shall be *"in lieu of all other taxes, duties, royalties, registration, license and other fees and charges, except only real property tax"*. The phrase *"in lieu of all other taxes"* includes, among others, those taxes that are *"directly due from or imposable upon the purchaser or the seller, producer, manufacturer, or importer of said petroleum products but are billed or passed on the grantee either as part of the price or cost thereof or by mutual agreement or other arrangement."*

Since PAL has direct and indirect tax exemptions under its franchise, it has the legal standing to file the claim for refund.

2. The withdrawal of PAL's tax exemption privileges in LOI No. 1483 covers only goods manufactured in the Philippines for domestic sales and not imported goods.

Thus, LOI No. 1483 amended PAL's franchise by withdrawing the tax exemption privilege granted to PAL on its *"purchase of domestic petroleum products for its use in its domestic operations."* This refers only to PAL's tax exemptions on passed-on excise tax costs due from the seller, manufacturer/producer of locally manufactured/produced goods for domestic sale and does not pertain to any of PAL's tax exemption privileges concerning imported goods.

**The City of Makati, represented by City Mayor,
the Hon. Jejomar C. Binay, et. al., vs.
Trans-Asia Power Generation Corporation**

CTA (Special First Division) AC Case No. 87 promulgated July 10, 2013

A company that operates, maintains, and manages a power plant for the conversion of fuel into electricity, which is in turn sold to customers, is classified as a manufacturer/producer for local business tax purposes.

Attorney's fees may be awarded when the city's act or omission compelled the taxpayer to litigate or to incur expenses to protect his interest.

Facts:

From 1996 to 2005, petitioner Makati City classified respondent Trans-Asia Power Generation Corporation (Trans-Asia) as a "Producer" for local business tax (LBT) purposes, and Trans-Asia paid the corresponding LBT.

In 2006, Makati City changed Trans-Asia's classification from "Manufacturer/Producer" to "Contractor/Services-Other Co." increasing the LBT assessed on the company. Trans-Asia paid the LBT under protest and requested Makati City to restore its original LBT classification as a "Producer." Trans-Asia also requested for the refund of alleged erroneously and illegally collected LBT arising from the reclassification.

As its protest remained unresolved, Trans-Asia filed with the Regional Trial Court of Makati City (RTC Makati) a civil action to protest the LBT assessment with a claim for refund against Makati City. Trans-Asia argued, among others, that the reclassification by Makati City from "Manufacturer/Producer" to "Contractor/Services-Other Co" was made without prior notice; hence, it was deprived of the opportunity to challenge the reclassification.

RTC Makati ruled in favor of Trans-Asia and ordered Makati City to refund the excess LBT and pay attorney's fees. Makati City filed a Petition for Review with the CTA.

Issues:

1. Is Trans-Asia entitled to a refund of erroneously paid LBT?
2. Is Trans-Asia entitled to attorney's fees?

Ruling:

1. Yes. Trans-Asia is entitled to a refund of excess LBT paid to Makati City; it is classified as a "Manufacturer/Producer" for LBT purposes.

Trans-Asia is primarily engaged in the business of, among others, building, erecting, owning, operating, maintaining, selling, leasing power generation plants, facilities, machineries and equipment; selling electricity generated by such power plants; and purchasing, importing, acquiring, owning, leasing power generation, transmission, telecommunications, transportation and other kinds of equipment, materials and facilities.

Trans-Asia's business operation falls within the purview of a "Manufacturer/Producer" under the Local Government Code of 1991 and the Makati Revenue Code. It was not disputed that Trans-Asia buys bunker fuel as its chief raw material and converts it through mechanical and chemical processes to electricity that is sold to its customer.

Moreover, the reclassification of Trans-Asia's status from "Producer" to "Services-Other Co." was made by Makati without any prior notice, which deprived Trans-Asia of the opportunity to challenge the reclassification to its prejudice.

2. Yes. Trans-Asia is entitled to attorney's fees.

Left with no recourse and if only to protect its interest, Trans-Asia was compelled to litigate to recover the overpaid LBT which Makati refused to refund. Trans-Asia is entitled to the award of attorney's fees under Article 2208(2) of the Civil Code which provides that attorney's fees may be awarded "when the defendant's act or omission has compelled the plaintiff to litigate with third persons or to incur expenses to protect his interest."

People of the Philippines vs. Efren O. Docena and Rolando E. Palad, South Sea Surety & Insurance Co., Inc.

Court of Tax Appeals (Special First Division)

Criminal Case No. 0-087 promulgated July 15, 2013

Facts:

Accused Efren O. Docena and Rolando E. Palad, then the President and Executive Vice President/Chief Operating Officer, respectively, of South Sea Surety & Insurance Co., Inc. (South Sea Surety) were charged with violation of Section 255 in relation to Sections 253(d) and 256 of the Tax Code, for alleged willful failure and refusal to pay deficiency DST and penalties for taxable year 2003.

The BIR issued a Final Assessment Notice and Formal Letter of Demand both dated May 9, 2005 against South Sea Surety for deficiency DST for taxable year 2003. South Sea Surety did not file a protest and the accused offered to settle the deficiency DST in six monthly installments. South Sea Surety then filed with the CIR an application for installment payment of deficiency tax assessed. It paid the first installment but did not pay the balance of the installment payments despite BIR request.

In a criminal case for willful and felonious failure to pay taxes, the prosecution must establish the guilt of the accused beyond reasonable doubt, by proving that the taxpayer is legally required to pay the assessed tax, and that the accused willfully and feloniously failed to pay the assessment at the time legally required to do so.

The BIR issued a Preliminary Collection letter and Warrant of Distraint and Levy to effect collection of the deficiency tax. Accused Palad submitted a promissory note with a schedule of payments. As South Sea Surety failed to make further payments, the BIR referred the accused for indictment of criminal charges. At this time, South Sea Surety had paid three installments although this fact was not disclosed to the Prosecutor.

During trial, accused Palad explained that he and his co-accused Docena did not willfully and unlawfully neglect to pay the tax liabilities of South Sea Surety. He responded to the notices sent by the BIR and filed an application for installment payment. He and Docena exerted their best efforts to settle the company's tax obligation.

Accused Palad explained that the payments stopped when the Office of the Insurance Commission directed South Sea Surety to cease and desist from transacting business. South Sea Surety was placed under receivership and the accused lost control of the management and operation of the company. Accused Palad also testified that the company was already in financial distress even before the BIR issued its deficiency tax assessment. He explained that the deficiency arose from agents who sold the insurance policies at reduced rates and pocketed portions belonging to the company. Another defense witness testified that he recommended the filing of the appropriate cases against the erring brokers and agents of the company.

Issue:

Are the accused Palad and Docena criminally liable for willful and felonious failure to pay tax to the BIR?

Ruling:

No. The accused are not criminally liable for willful and felonious failure to pay tax. However, as the responsible officers of South Sea Surety, they are civilly liable for the payment of the deficiency DST and compromise penalty to the government.

In a criminal case, the accused is presumed innocent until proven guilty. The prosecution must establish the guilt of the accused beyond reasonable doubt. Moral certainty is required, or that degree of proof which produces conviction in an unprejudiced mind.

The prosecution must prove the following elements of the crime charged:

- (1) That South Sea is, by law and regulations, required to pay the assessed DST.
- (2) That the accused Palad and Docena, as the responsible officers of the company, willfully and feloniously failed to pay the assessed DST.
- (3) That there was failure to pay at the time the accused were legally required to do so.

The facts of the case, together with the demeanor of accused Palad, do not instill belief that he and his co-accused willfully and feloniously failed and refused to pay the assessed DST and compromise penalty to the damage and prejudice of the government.

The term "willful" in tax crimes statutes means a "voluntary, intentional violation of a known legal duty and bad faith or bad purpose need not be shown." Moreover, "willfulness is a state of mind that may be inferred from the circumstances of the case. Proof of willfulness may be, and usually is, shown by circumstantial evidence alone.

In the present case, willfulness in the alleged failure and refusal of the accused to pay the assessed DST and compromise penalty is lacking to sustain a conviction. The evidence shows a pattern of affirmative acts on the attempt of South Sea Surety, through the accused, to pay the tax liability of the company amidst financial distress. These acts negate voluntary or purposeful intention, on the part of the accused, not to pay the tax liabilities of the company.

The primordial duty of the prosecution is not only to prove that a tax is due, but also to establish that the accused “willfully fails” to pay the tax due. The prosecution failed in the present case. Where the quantum of proof beyond reasonable doubt to warrant conviction of the accused for the offense charged was not established, accused should be acquitted.

However, while the accused cannot be held criminally liable as they were legally prevented from making further installments by virtue of the Cease and Desist Order of the Insurance Commission and the subsequent directive placing the corporation under receivership, the government still has the right to collect and be paid the remaining deficiency DST and compromise penalty assessed against South Sea Surety.

The accused are civilly liable, and are directed to jointly or severally pay, the unpaid portion of the assessed deficiency DST and compromise penalty, plus 20% deficiency interest from day of default until full payment.

Deutsche Bank AG Manila Branch vs. Commissioner of Internal Revenue

Supreme Court First Division

G.R. No. 188550 promulgated August 19, 2013

The failure to strictly comply with the requirement under RMO No. 1-2000 to file an application for TTRA 15 days prior to availing the provisions of a tax treaty, should not deprive a taxpayer of the benefit of a tax treaty.

The Supreme Court’s Minute Resolution in the *Mirant* case is not a binding precedent.

Facts:

On October 21, 2003, Petitioner Deutsche Bank AG Manila Branch (Deutsche Bank) remitted after-tax branch profits to its head office in Germany using the 15% branch profits remittance tax (BPRT) prescribed under the Tax Code. On October 4, 2005, believing that it overpaid the BPRT, Deutsche Bank filed –

- ▶ With the BIR Large Taxpayers Assessment and Investigation Division (LTAID) an administrative claim for refund or issuance of a tax credit certificate (TCC) for the difference between the 15% BPRT that it had paid in 2003, and the 10% BPRT rate prescribed under the RP-Germany Tax Treaty; and
- ▶ With the BIR International Tax Affairs Division (ITAD) a request for confirmation of its entitlement to the 10% BPRT rate under the RP-Germany Tax Treaty –

on the basis of paragraph 6, Article 10, of the RP-Germany Tax Treaty, which provides that where a resident of the Federal Republic of Germany has a branch in the Republic of the Philippines, this branch may be subjected to the BPRT withheld at source in accordance with Philippine law but shall not exceed 10% of the gross amount of the profits remitted by that branch to the head office.

On October 18, 2005, Deutsche Bank filed a Petition for Review with the CTA reiterating its claim for refund or issuance of a TCC for the amount of BPRT it had overpaid. The CTA denied the refund on the ground that the tax treaty relief (TTRA) was not filed with the BIR ITAD 15 days prior to the payment of the BPRT and actual remittance of the branch profits to Germany. RMO No. 1-2000 requires that any availing of the tax treaty relief must be preceded by an application with ITAD at least 15 days before the transaction. RMO No. 1-2000 was issued to streamline the processing of the application of tax treaty relief in order to improve efficiency and service to the taxpayers. Further, it also aims to prevent the consequences of an

erroneous interpretation and/or application of the treaty provisions (i.e., filing a claim for a tax refund/credit for the overpayment of taxes or for deficiency tax liabilities for underpayment).

Citing the *Mirant* case, the CTA En Banc held that a ruling from the BIR's ITAD must be secured prior to the availment of a preferential tax rate under a tax treaty. Applying the principle of *stare decisis et non quieta movere*, the CTA *En Banc* took into consideration that in Minute Resolutions dated 12 November 2007 and 18 February 2008, the Supreme Court denied the Petition filed by Mirant for failure to sufficiently show any reversible error in the assailed judgment. The CTA *En Banc* ruled that once a case has been decided in one way, any other case involving exactly the same point at issue should be decided in the same manner.

Deutsche Bank argued that, considering that it has met all the conditions under Article 10 of the RP-Germany Tax Treaty, the CTA erred in denying its claim solely on the basis of RMO No. 1-2000. The filing of a TTRA is not a condition precedent to the availment of a preferential tax rate. Deutsche Bank also argued that, contrary to the ruling of the CTA, *Mirant* is not a binding judicial precedent to deny a claim for refund solely on the basis of noncompliance with RMO No. 1-2000. On the other hand, Respondent CIR countered that the requirement of prior application under RMO No. 1-2000 is mandatory in character. RMO No. 1-2000 was issued pursuant to the unquestioned authority of the Secretary of Finance to promulgate rules and regulations for the effective implementation of the Tax Code. Thus, courts cannot ignore administrative issuances which partake the nature of a statute and have in their favor a presumption of legality.

Issues:

1. Is the failure to strictly comply with RMO No. 1-2000 sufficient to deprive persons or corporations of the benefit of a tax treaty?
2. Is the decision of the Court in *Mirant* a binding precedent?
3. Is Deutsche Bank entitled to the refund or TCC?

Ruling:

1. No. The failure to strictly comply with the requirement under RMO No. 1-2000 to file a TTRA 15 days prior to the availment of the provisions of a tax treaty should not deprive a taxpayer of the benefit of a tax treaty.

The crux of the controversy lies in the implementation of RMO No. 1-2000.

The Constitution provides for adherence to the general principles of international law as part of the law of the land. The time-honored international principle of *pacta sunt servanda* demands the performance in good faith of treaty obligations on the part of the states that enter into the agreement. Every treaty in force is binding upon the parties, and obligations under the treaty must be performed by them in good faith. More importantly, treaties have the force and effect of law in this jurisdiction. Tax treaties are entered into "to reconcile the national fiscal legislations of the contracting parties and, in turn, help the taxpayer avoid simultaneous taxations in two different jurisdictions."

"A state that has contracted valid international obligations is bound to make in its legislations those modifications that may be necessary to ensure the fulfillment of the obligations undertaken." Thus, laws and issuances must ensure that the reliefs granted under tax treaties are accorded to the parties entitled thereto. The BIR must not impose additional requirements that would negate the availment of

the reliefs provided for under international agreements. More so, when the RP-Germany Tax Treaty does not provide for any pre-requisite for the availment of the benefits under said agreement.

Likewise, there is nothing in RMO No. 1-2000 which would indicate a deprivation of entitlement to a tax treaty relief for failure to comply with the 15-day period. The Court said: "We recognize the clear intention of the BIR in implementing RMO No. 1-2000, but the CTA's outright denial of a tax treaty relief for failure to strictly comply with the prescribed period is not in harmony with the objectives of the contracting state to ensure that the benefits granted under tax treaties are enjoyed by duly entitled persons or corporations."

Bearing in mind the rationale of tax treaties, the period of application for the availment of tax treaty relief as required by RMO No. 1-2000 should not operate to divest entitlement to the relief as it would constitute a violation of the duty required by good faith in complying with a tax treaty. The denial of the availment of tax relief for the failure of a taxpayer to apply within the prescribed period under the administrative issuance would impair the value of the tax treaty. At most, the application for a tax treaty relief from the BIR should merely operate to confirm the entitlement of the taxpayer to the relief.

While the consequences sought to be prevented by RMO No. 1-2000 involve an administrative procedure, these may be remedied through other system management processes, e.g., the imposition of a fine or penalty. But we cannot totally deprive those who are entitled to the benefit of a treaty for failure to strictly comply with an administrative issuance requiring prior application for tax treaty relief.

2. No, the Supreme Court's Minute Resolution in *Mirant* is not a binding precedent.

The Court has clarified this matter in *Philippine Health Care Providers, Inc. v. Commissioner of Internal Revenue* (G.R. No. 167330, 18 September 2009, 600 SCRA 413) as follows:

"It is true that, although contained in a minute resolution, our dismissal of the petition was a disposition of the merits of the case. When we dismissed the petition, we effectively affirmed the CA ruling being questioned. As a result, our ruling in that case has already become final. When a minute resolution denies or dismisses a petition for failure to comply with formal and substantive requirements, the challenged decision, together with its findings of fact and legal conclusions, are deemed sustained. But what is its effect on other cases?

With respect to the same subject matter and the same issues concerning the same parties, it constitutes *res judicata*. However, if other parties or another subject matter (even with the same parties and issues) is involved, the minute resolution is not binding precedent."

Besides, there are substantial, not simply formal, distinctions between a minute resolution and a decision. The constitutional requirement under the first paragraph of Section 14, Article VIII of the Constitution that the facts and the law on which the judgment is based must be expressed clearly and distinctly applies only to decisions, not to minute resolutions. A minute resolution is signed only by the clerk of court by authority of the justices, unlike a decision. It does not require the certification of the Chief Justice. Moreover, unlike decisions, minute resolutions are not published in the Philippine Reports. Finally, the *proviso* of Section 4(3) of Article VIII speaks of a decision. Indeed, as a rule, this Court lays down doctrines or principles of law which constitute binding precedent in a decision duly signed by the members of the Court and certified by the Chief Justice.

Even if we had affirmed the CTA in *Mirant*, the doctrine laid down in that Decision cannot bind this Court in cases of a similar nature. There are differences in parties, taxes, taxable periods, and treaties involved; more importantly, the disposition of that case was made only through a minute resolution.

3. Yes, Deutsche Bank is entitled to the refund or TCC.

RMO No. 1-2000 was implemented to obviate any erroneous interpretation and/or application of the treaty provisions. The objective of the BIR is to forestall assessments against corporations who erroneously availed themselves of the benefits of the tax treaty but are not legally entitled thereto, as well as to save such investors from the tedious process of claims for a refund due to an inaccurate application of the tax treaty provisions. However, noncompliance with the 15-day period for prior application should not operate to automatically divest entitlement to the tax treaty relief especially in claims for refund.

The underlying principle of prior application with the BIR becomes moot in refund cases, such as the present case, where the very basis of the claim is erroneous or there is excessive payment arising from non-availment of a tax treaty relief at the first instance. In this case, petitioner should not be faulted for not complying with RMO No. 1-2000 prior to the transaction. It could not have applied for a tax treaty relief within the period prescribed, or 15 days prior to the payment of its BPRT, precisely because it erroneously paid the BPRT not on the basis of the preferential tax rate under the RP-Germany Tax Treaty, but on the regular rate as prescribed by the Tax Code. Hence, the prior application requirement becomes illogical. Therefore, the fact that Deutsche Bank invoked the provisions of the RP-Germany Tax Treaty when it requested for a confirmation from the ITAD before filing an administrative claim for a refund should be deemed substantial compliance with RMO No. 1-2000.

Section 229 of the Tax Code provides the taxpayer a remedy for tax recovery when there has been an erroneous payment of tax. The outright denial of petitioner's claim for a refund, on the sole ground of failure to apply for a tax treaty relief prior to the payment of the BPRT, would defeat the purpose of Section 229.

It is significant to emphasize that petitioner applied - though belatedly - for a tax treaty relief, in substantial compliance with RMO No. 1-2000. A ruling by the BIR would have confirmed whether petitioner was entitled to the lower rate of 10% BPRT pursuant to the RP-Germany Tax Treaty. Nevertheless, even without the BIR ruling, the CTA Second Division found that based on the evidence presented, both documentary and testimonial, petitioner was able to establish the following facts:

- a. That petitioner is a branch office in the Philippines of Deutsche Bank AG, a corporation organized and existing under the laws of the Federal Republic of Germany;
- b. That on October 21, 2003, it filed its Monthly Remittance Return of Final Income Taxes Withheld under BIR Form No. 1601-F and remitted the amount of P67,688,553.51 as BPRT with the BIR; and
- c. That on October 29, 2003, the *Bangko Sentral ng Pilipinas* having issued a clearance, petitioner remitted to Frankfurt Head Office the amount of Euro5,174,847.38 (or PhP330,175,961.88).

Likewise, both the administrative and the judicial actions were filed within the two-year prescriptive period pursuant to Section 229 of the Tax Code. Clearly, there is no reason to deprive petitioner of the benefit of a preferential tax rate of 10% BPRT in accordance with the RP-Germany Tax Treaty.

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