Tax Bulletin

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Highlights

BIR Issuances

- Revenue Memorandum Circular (RMC) No. 116-2019 clarifies the tax treatment of alien individuals employed in the Philippines by Regional or Area Headquarters (RHQs) and Regional Operating Headquarters (ROHQs) of Multinational Companies, Offshore Banking Units (OBUs) and Petroleum Service Contractors and Subcontractors pursuant to Section 4.C of RR No. 8-2018. **(Page 3)**

- RMC No. 117-2019 amends Section II of RMC No. 28-2019 relative to the use of BIR Printed Receipts/Invoices. **(Page 3)**

Court Decisions

- Underdeclaration of purchases does not, by itself, result in the imposition of income tax and VAT since no deficiency tax assessment can be made on account of undeclared purchases.

  A taxpayer is free to deduct from its gross income a lesser amount, or not claim any deduction at all. What is prohibited by the income tax law is to claim a deduction beyond the authorized amount, not an underdeclaration of purchases or unaccounted expenses. **(Page 4)**

- The sales by PSALM of the NPC's generating assets or power plants are not subject to VAT since the sales are not made in pursuit of a commercial or economic activity, but of a governmental function mandated by the EPIRA Law in order to privatize NPC generation assets. **(Page 5)**

- The Court of Tax Appeals (CTA)'s appellate jurisdiction is not limited to cases relating to assessments or refunds. The CTA may also take cognizance of "other matters" under the National Internal Revenue Code (NIRC) or other laws administered by the BIR, including the CIR's power to abate a tax liability. The BIR may summarily enforce collection, only when it has accorded the taxpayer administrative due process, which includes the issuance of a valid assessment. **(Page 6)**

- A taxpayer is allowed to claim deductions from its gross income to compute its taxable income subject to income tax. What is prohibited by the income tax law is a deduction beyond the authorized amount.

  The application of the Net Operating Loss Carry-Over (NOLCO), Minimum Corporate Income Tax (MCIT) and excess credits in subsequent taxable periods is beyond the scope of the present assessment. The same can only be the subject of assessment on the taxable year when they are claimed as deductions. **(Page 8)**

- Apart from payment of the Capital Gains Tax (CGT) and Documentary Stamp Tax (DST), the law does not impose any other condition before one is considered to have settled its tax obligations for the sale or transfer of real property. The requirements for the issuance of the CAR should be delineated from the tax obligations inherent in the sale or transfer of property. **(Page 9)**

BIR Issuances

RMC No. 116-2019 clarifies the tax treatment of alien individuals employed in the Philippines by RHQs and ROHQs of Multinational Companies, OBUs and Petroleum Service Contractors and Subcontractors pursuant to Section 4.C of RR No. 8-2018.

RMC No. 116-2019 issued on 6 November 2019

- The incomes of alien individuals employed by RHQs, ROHQs, OBUs and Petroleum Service Contractors are now taxed similarly to the income of regular employees of locally established entities.
- Thus, these alien individuals are subject to the same administrative requirements applicable to other regular employees, such as, among others, the substituted filing, issuance of BIR Form No. 2316, inclusion in the monthly withholding tax remittance on compensation and in the prescribed alphalists
- Alien individuals, who are employed by foreign principals and are assigned to render services exclusively to local entities ("seconded employees or secondees"), are also subject to the regular income tax rates.
    1. Their income derived from these services shall be taxable in the Philippines, regardless of whether their salary is paid by the foreign principal or advanced by the local entity.
    2. They are also subject to the same administrative requirements, except for the substituted filing.
    3. They shall file their annual income tax return and pay the income tax due, if applicable, on or before April 15 of each year, together with BIR Form No. 2316 duly issued by the local entities.
- In case their services are terminated before the end of the taxable year, the local entities shall ensure that the withholding tax on the last salaries shall be computed using the annualized withholding tax method.

RMC No. 117-2019 amends Section II of RMC No. 28-2019 relative to the use of BIR Printed Receipts/Invoices.

RMC No. 117-2019 issued on 6 November 2019

- New Business Registrants may immediately commence business operations upon buying BIR printed receipts/invoices (BPR/BPI) from the New Business Registrant Counter (NBRC) at the time of registration, in lieu of securing an Authority to Print (ATP) principal receipts/invoices.
- The BPR/BPI may be used on the first year of business operation or until its full consumption, whichever comes first.
- New business registrants who opted to use BPR/BPI during its first year of business operations are required to secure an ATP principal receipts/invoices beginning its second year of operations or before the remaining BPRs/BPIs are fully consumed, whichever comes later.
- Taxpayers whose business transactions will require the use of not more than one booklet of fifty sets in one taxable period (not less than twelve months) shall be allowed to buy BPR/BPI even beyond the one-year period from the date of business registration with the Bureau.

- The BPR/BPI shall be issued as principal evidence in the sale of goods and/or properties and/or services or lease of properties. It can also be used as a supporting document in claiming expenses as deduction from ordinary gross income or to claim input tax credit, subject to existing rules and regulations on invoicing requirements for taxation purposes.
- An ATP for supplementary receipts/invoices is required, if the new business registrants shall use supplementary receipts/invoices.

Court Decisions

Commissioner of Internal Revenue vs. Philippine Power MC Distribution, Inc.
CTA EB No. 1940 (CTA Case No. 9263) promulgated on 16 October 2019

Underdeclaration of purchases does not, by itself, result in the imposition of income tax and VAT since no deficiency tax assessment can be made on account of undeclared purchases.

A taxpayer is free to deduct from its gross income a lesser amount, or not claim any deduction at all. What is prohibited by the income tax law is to claim a deduction beyond the authorized amount, not an underdeclaration of purchases or unaccounted expenses.

Facts:

Philippine Power MC Distribution, Inc. (PPMDI), a domestic corporation, was assessed deficiency income tax and VAT for fiscal year (FY) ending 30 June 2008 due to its alleged undeclared purchases. After filing a protest against the deficiency tax assessments, it received a Final Decision on Disputed Assessment (FDDA), which demanded payment of deficiency VAT and income tax. PPMDI filed a Request for Reconsideration with the CIR, which was subsequently denied.

Aggrieved, PPMDI filed a Petition for Review with the CTA.

The Court in Division cancelled the CIR's deficiency tax assessments on the ground, among others, that the underdeclared purchases cannot be presumed to be an underdeclared income.

Issues:

Is PPMDI liable for deficiency income tax and VAT for taxable year 2008?

Rulings:

No. The alleged discrepancy/underdeclared purchases cannot constitute an undeclared income.

Three elements are necessary to impose tax, namely: (a) there must be gain or profit; (b) the gain or profit is realized or received, actually or constructively; and (c) it is not exempted by law or treaty. Therefore, income tax is assessed on income, which is received from any property, activity or service. It must also be clearly established that the taxpayer received such income. This condition is not present in this case. The CIR failed to establish by clear and convincing evidence, other than his alleged under-declared purchases, that PPMDI received an income that it did not declare in its return.

The same is true for VAT, which is based either on the gross selling price or gross value in money of the goods or properties sold, bartered or exchanged, or gross receipts derived from the sale or exchange of services.

A finding of underdeclaration of purchases does not by itself result in the imposition of income tax and VAT, since no deficiency tax assessment can be made on account of undeclared purchases.

A taxpayer is free to deduct from its gross income a lesser amount, or not claim any deduction at all. What is prohibited by the income tax law is to claim a deduction beyond the authorized amount, not an under-declaration of purchases or unaccounted expenses.

While all presumptions are in favor of the correctness of tax assessments, the assessment itself should not be based on presumptions no matter how logical the presumption might be. In order to stand the test of judicial scrutiny, the assessment must be based on actual facts.

Power Sector Assets and Liabilities Management Corporation vs. Commissioner of Internal Revenue
Supreme Court (Second Division) G.R. No. 226556, promulgated 3 July 2019

The sales by PSALM of the NPC's generating assets or power plants are not subject to VAT since the sales are not made in pursuit of a commercial or economic activity, but of a governmental function mandated by the EPIRA Law in order to privatize NPC generation assets.

Facts:

The Power Sector Assets and Liabilities Management Corporation (PSALM), a government-owned and controlled corporation created under the Electric Power Industry Reform Act of 2001 (or EPIRA Law), is mandated to manage the orderly sale, disposition, and privatization of the National Power Corporation's (NPC's) generation assets, real estate and other disposable assets, and Independent Power Producer contracts with the objective of liquidating all NPC financial obligations and stranded contract costs in an optimal manner.

The BIR assessed PSALM for deficiency VAT for the year 2008, alleging that PSALM's sales of generating assets (power plants), lease of the Naga Complex, collection of income and receivables should be subject to the 12% VAT.

PSALM filed its protest, arguing that the privatization of the NPC's assets is an original mandate of PSALM and hence, the above transactions are not subject to VAT.

Upon denial of the protest, PSALM appealed to the CTA, which ruled that the sale of generating assets of PSALM is subject to VAT since this was done in the course of PSALM's trade or business, and that the Tax Code, as amended by Republic Act No. 9337, placed the electric power industry under the VAT system.

Issue:

Are the sales of generating assets (power plants) by PSALM subject to VAT?

Ruling:

No, the sales are not subject to VAT.

This issue has been passed upon in the 2017 case of *PSALM vs. Commissioner of Internal Revenue*, where the Court ruled that the BIR's position is anchored on the wrong premise that PSALM is a successor-in-interest of the NPC.

Under its charter, the NPC is mandated to "undertake the development of hydroelectric generation of power and the production of electricity from nuclear, geothermal and other sources, as well as the transmission of electric power on a nationwide basis." Under the EPIRA Law, which restructured the electric power industry into generation, transmission, distribution, and supply sectors, the NPC is now primarily mandated to perform missionary electrification functions. PSALM, on the other hand, was created to liquidate all of the NPC's financial obligations.

PSALM is not a successor-in-interest of the NPC and therefore, the repeal of the NPC's VAT exemption does not affect PSALM.

Even if PSALM is deemed a successor-in-interest of the NPC, still the sale of the power plants is not "in the course of trade or business" as contemplated by the Tax Code and, is therefore, not subject to VAT.

The sale of the power plants is not in pursuit of a commercial or economic activity, but of a governmental function mandated by law to privatize NPC generation assets. The sale of the power plants is clearly not the same as the sale of electricity by generation, transmission, and distribution companies, which is subject to VAT under the Tax Code.

This is similar to the 2006 case of *Magsaysay Lines* where the Court ruled that the sale of vessels of the National Development Company to Magsaysay Lines is not subject to VAT since it was not made in the course of trade or business, as it was involuntary and made pursuant to the government's policy of privatization.

PSALM is also not liable to pay VAT on the following activities: a) lease of the Naga Complex; b) collection of income from participation fees, site visit fees, plant CDs, photocopying charges and data room access fees; and c) collection of receivables from employees for the excess utilization of allowed mobile phone services, inventory variance receivables from the custodian, refunds from a successor-generation company of the insurance premiums paid by PSALM and interest from mandatory dollar deposits.

Under the EPIRA Law, PSALM, as the conservator of NPC assets, operated and maintained NPC assets and manages its liabilities in trust for the national government until the NPC assets could be sold or disposed of. Thus, during its corporate life, PSALM has powers relating to the management of its personnel and leasing of its properties as may be necessary to discharge its mandate.

Since the lease of the NAGA Complex and the collection of income and receivables are within PSALM's powers, which are necessary to discharge its mandate under the law, and likewise undertaken in the exercise of PSALM's governmental function, these activities are not subject to VAT.

Commissioner of Internal Revenue vs. Pacific Hub Corporation
CTA (*En Banc*) Case Nos. 1837, promulgated 8 November 2019

The CTA's appellate jurisdiction is not limited to cases relating to assessments or refunds. The CTA may also take cognizance of "other matters" under the NIRC or other laws administered by the BIR, including the CIR's power to abate a tax liability.

The BIR may summarily enforce collection, only when it has accorded the taxpayer administrative due process, which includes the issuance of a valid assessment.

Facts:

Respondent Pacific Hub Corporation ("PHC") filed an application for abatement for taxable years 2005 and 2006 after failing to pay the full amounts due based on the withholding tax on compensation (WTC), expanded withholding tax (EWT), and VAT returns it filed. Citing continued financial losses, PHC requested the Petitioner CIR to cancel the penalties, surcharge and interest in July 2009. In January 2010, PHC paid the basic WTC, EWT and VAT due amounting to P15,480,231.11.

The CIR issued a Notice of Denial dated 10 January 2014, which PHC received on 20 August 2014. The CIR then issued a Warrant of Distraint and/ or Levy to enforce the collection of the unpaid increments.

PHC filed a Petition for Review with the CTA assailing the validity of the denial and the enforcement procedure.

The CIR questioned the CTA's jurisdiction to hear the case, arguing that no decision on disputed assessment has been issued which could be the subject of review by the CTA. It also averred that the BIR complied with all the requirements laid down in the Tax Code and implementing issuances in denying the abatement application.

The CTA 3rd Division nullified the Notice of Denial for failing to state the reasons for the disapproval of the request for abatement, as required under Section 4 of Revenue Regulations No. 13-2001. The issuance of the Warrant of Distraint and/or Levy was, likewise, voided.

Aggrieved, the BIR filed a Petition for Review with the CTA *En Banc*.

Issues:

1. Can the CTA review the BIR's denial of the abatement application?

2. Is the Warrant of Distraint and/or Levy valid?

3. Is the Notice of Denial void?

Rulings:

1. Yes. The CTA's appellate jurisdiction is not limited to cases relating to assessments or refunds and there are "other matters" under the NIRC or other laws administered by the BIR that the CTA may take cognizance of. The authority of the Commissioner to abate or cancel a tax liability is provided under Sec. 204 of the NIRC.

   While it is generally true that purely administrative and discretionary functions may not be interfered with by the courts, the CTA *En Banc* held that any decision by the CIR in relation to the exercise of the power to abate or cancel a tax liability tainted by a failure to abide by the command of the law (i.e., failure to cite the basis for denial, as mandated by RR 13-2001) is subject to the CTA's exclusive appellate jurisdiction.

2. No. Citing the Supreme Court's ruling in *CIR vs. Pilipinas Shell Petroleum Corporation, GR No. 197945 promulgated on 9 July 2018*, the BIR must first make an assessment and, then, enforce the collection of the amounts so assessed. An assessment is a step preliminary, but essential to a warrant of distraint. The BIR may summarily enforce collection, only when it has accorded the taxpayer administrative due process, which includes the issuance of a valid assessment. In this case, there is no evidence on record to show that an assessment was ever issued, prior to the issuance of the Warrant of Distraint and/or Levy.

3. Yes. The Notice of Denial failed to state any reason for its disapproval, contrary to the explicit requirement of Sec.4 of RR 13-2001. It merely stated that PHC's application for abatement has been disapproved.

A taxpayer is allowed to claim deductions from its gross income to compute its taxable income subject to income tax. What is prohibited by the income tax law is a deduction beyond the authorized amount.

The application of the NOLCO, MCIT and excess credits in subsequent taxable periods is beyond the scope of the present assessment. The same can only be the subject of assessment on the taxable year when they are claimed as deductions.

Commissioner of Internal Revenue vs. Alpha 245, Incorporated (formerly, Arc Worldwide Philippines Co. Inc.)
CTA (*En Banc*) Case No. 1875 promulgated 1 October 2019

Facts:

Petitioner CIR assessed Respondent Alpha 245, Inc. ("Alpha 245") for various deficiency taxes for taxable year 2009. Upon the filing of a protest, the BIR requested Alpha 245 to submit the supporting documents and failing to receive any, issued a Final Decision on Disputed Assessment. Alpha 245 filed a request for reconsideration and submitted its audited financial statements and income tax return for 2009 and 2010. The BIR denied the request for reconsideration, arguing that Alpha 245 did not submit the required supporting documents within the 60-day period.

Alpha 245 filed a Petition for Review at the CTA.

The CIR argued that it was able to establish that Alpha 245's operations showed a taxable income instead of net operating loss, as claimed by the Company in its 2009 ITR. On this basis, the CIR added back Alpha 245's net operating loss under the presumption that the tax benefit has already been forwarded to succeeding periods. It also disallowed the Minimum Corporate Income Tax (MCIT) and the excess creditable withholding taxes at the end of the taxable year 2009.

The CTA 2nd Division cancelled the Income Tax assessment for lack of basis, considering that the computation of Alpha 245's taxable income per investigation results in a net loss. It also ruled that Alpha 245 cannot be presumed to have undeclared income due to its undeclared rent expense. The EWT and DST, including increments, were already duly paid. The deficiency VAT assessment was upheld as there was portion of its gross receipts that was not duly subjected to VAT.

Upon denial of their respective motions for reconsideration, both parties filed a Petition for Review at the CTA *En Banc*.

Issues:

1. Is Alpha 245 liable for deficiency income tax on account of its undeclared rent expense which presumably resulted in undeclared income?

2. Can the BIR disallow the application of NOLCO, MCIT and excess CWTs?

Rulings:

1. No. For income tax purposes, a taxpayer is allowed to claim deductions from its gross income to compute its taxable income subject to income tax. What is prohibited by the income tax law is a deduction beyond the authorized amount. The imputation of alleged undeclared income is based on a mere presumption that since there are undeclared expenses (i.e., rent), there are corresponding undeclared sources of income. Even if these alleged unaccounted expenses are to be treated as undeclared income, the same will be offset by recording the equivalent payments as expenses. As such, there will be no resulting taxable income on these transactions.

2. No. The application of the NOLCO, MCIT and excess credits in the subsequent taxable periods is beyond the scope of the present assessment. The same can only be the subject of assessment on the taxable year when they are claimed as deductions.

   Alpha 245 submitted its ITR for 2010, 2011, and 2012, which showed that it suffered net operating losses for these years. In 2011, it applied the NOLCO from 2008. The NOLCO from 2009, as supported by the 2012 ITR, remains unapplied and has expired. The CTA *En Banc* ruled that it was erroneous for the BIR to add the net loss back to the taxable period per investigation and to disallow MCIT and excess tax credits.

East West Banking Corporation vs. Commissioner of Internal Revenue and the Revenue Officer of Revenue District Office No. 57 – City of Binan, Bureau of Internal Revenue
CTA (First Division) Case No. 9762 promulgated 3 October 2019

Apart from payment of the CGT and DST, the law does not impose any other condition before one is considered to have settled its tax obligations for the sale or transfer of real property. The requirements for the issuance of the CAR should be delineated from the tax obligations inherent in the sale or transfer of property.

Facts:

Petitioner East West Banking Corporation ("Eastwest") filed a claim for refund on 17 January 2018 of erroneously paid Capital Gains Tax (CGT) and Documentary Stamp tax (DST) on 3 parcels of land acquired from defaulting bank borrowers.

In the course of securing Certificates Authorizing Registration (CARs) for the acquired properties, the BIR required Eastwest to submit copies of the CARs for previous transfers of the same land parcels. As it cannot produce the CARs and in order to consolidate title over the properties, Eastwest nonetheless paid the CGT and DST on previous transfers on 28 and 29 January 2016.

Due to the inaction of the BIR and to toll the 2-year prescriptive period, Eastwest file a Petition for Review at the Court of Tax Appeals on 26 January 2018.

At the CTA, the BIR anchored its position on Revenue Memorandum Circular 76-2007, which requires either (1) a certified true copy of the original CAR pertaining to the transfer of property prior to the issuance of the title, which is the subject of the current transfer; or (2) a certification by the Registry of Deeds with the pertinent details of the CAR before a real property can be transferred.

Eastwest argued that Section 27(D)(5) of the NIRC, as amended, only requires the payment of CGT on the gains realized in the sale, exchange, or disposition of lands. There is no obligation on the parties to pay the CGT on the previous transactions involving the same property. Moreover, the requirement to submit the previous CAR before the transfer of title to a property is unreasonable and oppressive.

Issues:

1. Can the BIR require a taxpayer to settle the CGT and DST on a previous transfer of real property before the issuance of a CAR for the current sales transaction?

2. Is Eastwest eligible to a refund of erroneously paid CGT and DST?

Rulings:

1. No. There is no law which imposes CGT and DST on previous transfers of real property to parties to a current sales transaction involving the same real property. The requirements under RMC 76-2007, as later amended by RMC 105-2016, speak of conditions before a CAR will be issued in order for the Register of Deeds to effect a change in the names registered in the title of the property. These requirements embodied in such circulars must be distinguished from a tax obligation provided by law in case of transfer of real property, e.g., payment of CGT and DST.

   Section 27(D)(5) and Section 196 of the NIRC, as amended, provide only for a single payment of CGT and DST on *each* sale of real property. Apart from payment of the CGT and DST, the law does not impose any other condition before one is considered to have settled its tax obligations for the sale or transfer of real property. The requirements for the issuance of the CAR should be delineated from the tax obligations inherent in the sale or transfer of property.

2. Yes. The payment of CGT and DST for prior transactions is not sanctioned by law, hence the payment is considered erroneous and must be refunded. Eastwest was constrained to pay CGT and DST on the previous transfer only to expedite the consolidation of its title over the subject properties. Citing the Supreme Court case of *CIR vs. Mirant Pagbilao Corporation, GR No. 172129 promulgated on 12 September 2008*, the CTA held that the return of what was erroneously paid is founded on the principle of *solution indebiti*, or the principle that no one should unjustly enrich himself at the expense of another. As Eastwest complied with all the requisites for the filing of the refund, including the application with the 2-year period, it is eligible for a refund.

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