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TAX TREATY

A BACKGROUNDER*

In the grand scheme of the present generation's economic activities, governments of countries having political jurisdiction of different territories rely on each other to solve and resolve the myriad and complex issues confronting world trade and the exchange of goods and services. One vital tool being utilized is the entering into tax concessions or agreements between contracting countries. This is popularly known as *Tax Treaties*. These conventions are formal agreements between sovereign states that confer rights and obligations to the contracting states and to persons covered by such treaties.[1] They are entered into mainly by the parties to avoid international multiple or double taxation, deter tax avoidance, and prevent fiscal evasion. These hindrances may likewise be reduced by providing for allowance of deduction or tax credit of foreign taxes via act of Congress.

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* **Prepared by : Mr. Clinton S. Martinez**
SLSO-II, ODG

[1] Mamalateo, V.C. (2010). Philippine Tax Treaties, p. 2-3.

"*Exemptions from taxation by treaty are generally granted on the grounds of reciprocity and to lessen the rigors of international double taxation and multiple taxation*." (Vitug: Reviewer in Taxation, p. 54)

Double taxation takes place when a person or corporation who owns or derives income from two or more jurisdictions is taxed by said taxing authorities on said properties separately and individually. To avoid this practice, States enter into Tax Treaties or Conventions. Reciprocal treatment is expected from member States for the orderly implementation of the pacts.

Treaties have *come to denote any international agreement intended to have an obligatory character*.[2] They are a meeting of the minds between States. Treaties have also been defined as a *formal instrument of agreement by which two or more States establish or seek to establish a relation under international law between themselves*.[3] The recently enacted Customs Modernization and Tariff Act [(CMTA), RA 10863, May 30, 2016] was passed, in part, in conformity with our international trade and tariff commitments.

For these tax treaties or conventions to be valid and effective, the ensuing provision of the 1987 Philippine Constitution must be observed:

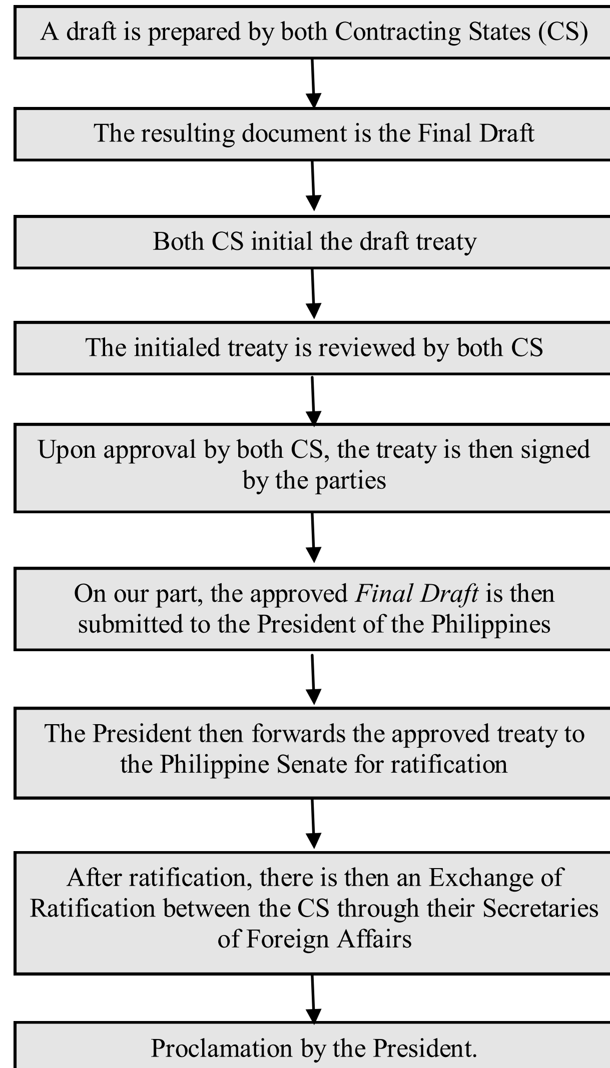
> *"Section 21. No treaty or international agreement shall be valid and effective unless concurred in by at least two-thirds of all the Members of the Senate."* (Article VII, Executive Department)

In relation to the above, the same Constitution provides:

> "*Section 2. The Philippines renounces war as an instrument of national policy, adopts the generally accepted principles of international law as part of the law of the land and adheres to the policy of peace, equality, justice, freedom, cooperation, and amity with all nations."* (Article II, Declaration of Principles and State Policies)

Under Section 32(B)(5) of the National Internal Revenue Code (NIRC), as amended, income exempt under treaty are excluded from the computation of the gross income.

The tedious process of entering into a tax treaty may be summarized as follows:



> *The treaty becomes effective on the first day of January of the year following the exchange of Instruments of Ratification, because tax treaties are self-executing and they become operative as domestic law in the Philippines without the necessity of enabling legislation*." [4]

A Tax Treaty has the following typical contents:[5]

SUMMARY OF THE CONVENTION
TITLE AND PREAMBLE

CHAPTER I
Scope of the Convention

Article 1
Persons Covered

This Convention shall apply to persons who are residents of one or both of the Contracting States.

[2] Sibal, J.A.S. (1986). Philippine Legal Encyclopedia (p. 1079).

[3] Article 1, Harvard Draft Convention, cited in Sibal, supra.

[4] Mamalateo, V.C. (2010). Philippine Tax Treaties, p. 5.

[5] Source: http://www.oecd.org/tax/treaties; Organization for Economic Cooperation and Development (OECD) Model Tax Convention

Article 2
Taxes covered

1. This Convention shall apply to taxes on income and on capital imposed on behalf of a Contracting State or of its political subdivisions or local authorities, irrespective of the manner in which they are levied.

2. There shall be regarded as taxes on income and on capital all taxes imposed on total income, on total capital, or on elements of income or of capital, including taxes on gains from the alienation of movable or immovable property, taxes on the total amounts of wages or salaries paid by enterprises, as well as taxes on capital appreciation.

3. The existing taxes to which the Convention shall apply are in particular: a) (in State A): .... b) (in State B): ....

4. The Convention shall apply also to any identical or substantially similar taxes that are imposed after the date of signature of the Convention in addition to, or in place of, the existing taxes. The competent authorities of the Contracting States shall notify each other of any significant changes that have been made in their taxation laws.

CHAPTER II
Definitions

Article 3
General Definitions

1. For the purposes of this Convention, unless the context otherwise requires:

a) the term "person" includes an individual, a company and any other body of persons;

b) the term "company" means any body corporate or any entity that is treated as a body corporate for tax purposes;

c) the term "enterprise" applies to the carrying on of any business;

d) the terms "enterprise of a Contracting State" and "enterprise of the other Contracting State" mean respectively an enterprise carried on by a resident of a Contracting State and an enterprise carried on by a resident of the other Contracting State;

e) the term "international traffic" means any transport by a ship or aircraft operated by an enterprise that has its place of effective management in a Contracting State, except when the ship or aircraft is operated solely between places in the other Contracting State;

f) the term "competent authority" means: (i) (in State A): .... (ii) (in State B): ....

g) the term "national", in relation to a Contracting State, means: (i) any individual possessing the nationality or citizenship of that Contracting State; and (ii) any legal person, partnership or association deriving its status as such from the laws in force in that Contracting State;

h) the term "business" includes the performance of professional services and of other activities of an independent character.

2. As regards the application of the Convention at any time by a Contracting State, any term not defined therein shall, unless the context otherwise requires, have the meaning that it has at that time under the law of that State for the purposes of the taxes to which the Convention applies, any meaning under the applicable tax laws of that State prevailing over a meaning given to the term under other laws of that State.

Article 4
Resident

1. For the purposes of this Convention, the term "resident of a Contracting State" means any person who, under the laws of that State, is liable to tax therein by reason of his domicile, residence, place of management or any other criterion of a similar nature, and also includes that State and any political subdivision or local authority thereof. This term, however, does not include any person who is liable to tax in that State in respect only of income from sources in that State or capital situated therein.

2. Where by reason of the provisions of paragraph 1 an individual is a resident of both Contracting States, then his status shall be determined as follows: a) he shall be deemed to be a resident only of the State in which he has a permanent home available to him; if he has a permanent home available to him in both States, he shall be deemed to be a resident only of the State with which his personal and economic relations are closer (centre of vital interests); b) if the State in which he has his centre of vital interests cannot be determined, or if he has not a permanent home available to him in either State, he shall be deemed to be a resident only of the State in which he has an habitual abode; c) if he has an habitual abode in both States or in neither of them, he shall be deemed to be a resident only of the State of which he is a national; d) if he is a national of both States or of neither of them, the competent authorities of the Contracting States shall settle the question by mutual agreement.

3. Where by reason of the provisions of paragraph 1 a person other than an individual is a resident of both Contracting States, then it shall be deemed to be a resident only of the State in which its place of effective management is situated.

Article 5
Permanent Establishment

1. For the purposes of this Convention, the term "permanent establishment" means a fixed place of business through which the business of an enterprise is wholly or partly carried on.

2. The term "permanent establishment" includes especially: a) a place of management; b) a branch; c) an office; d) a factory; e) a workshop, and f) a mine, an oil or gas well, a quarry or any other place of extraction of natural resources.

3. A building site or construction or installation project constitutes a permanent establishment only if it lasts more than twelve months.

4. Notwithstanding the preceding provisions of this Article, the term "permanent establishment" shall be deemed not to include: a) the use of facilities solely for the purpose of storage, display or delivery of goods or merchandise belonging to the enterprise; b) the maintenance of a stock of goods or merchandise belonging to the enterprise solely for the purpose of storage, display or delivery; c) the maintenance of a stock of goods or merchandise belonging to the enterprise solely for the purpose of processing by another enterprise; d) the maintenance of a fixed place of business solely for the purpose of purchasing goods or merchandise or of collecting information, for the enterprise; e) the maintenance of a fixed place of business solely for the purpose of carrying on, for the enterprise, any other activity of a preparatory or auxiliary character; f) the maintenance of a fixed place of business solely for any combination of activities mentioned in subparagraphs a) to e), provided that the overall activity of the fixed place of business resulting from this combination is of a preparatory or auxiliary character.

5. Notwithstanding the provisions of paragraphs 1 and 2, where a person — other than an agent of an independent status to whom paragraph 6 applies — is acting on behalf of an enterprise and has, and habitually exercises, in a Contracting State an authority to conclude contracts in the name of the enterprise, that enterprise shall be deemed to have a permanent establishment in that State in respect of any activities which that person undertakes for the enterprise, unless the activities of such person are limited to those mentioned in paragraph 4 which, if exercised through a fixed place of business, would not make this fixed place of business a permanent establishment under the provisions of that paragraph.

6. An enterprise shall not be deemed to have a permanent establishment in a Contracting State merely because it carries on business in that State through a broker, general commission agent or any other agent of an independent status, provided that such persons are acting in the ordinary course of their business.

7. The fact that a company which is a resident of a Contracting State controls or is controlled by a company which is a resident of the other Contracting State, or which carries on business in that other State (whether through a permanent establishment or otherwise), shall not of itself constitute either company a permanent establishment of the other.

CHAPTER III
Taxation of Income

Article 6
Income From Immovable Property

1. Income derived by a resident of a Contracting State from immovable property (including income from agriculture or forestry) situated in the other Contracting State may be taxed in that other State.

2. The term "immovable property" shall have the meaning which it has under the law of the Contracting State in which the property in question is situated. The term shall in any case include property accessory to immovable property, livestock and equipment used in agriculture and forestry, rights to which the provisions of general law respecting landed property apply, usufruct of immovable property and rights to variable or fixed payments as consideration for the working of, or the right to work, mineral deposits, sources and other natural resources; ships, boats and aircraft shall not be regarded as immovable property.

3. The provisions of paragraph 1 shall apply to income derived from the direct use, letting, or use in any other form of immovable property.

4. The provisions of paragraphs 1 and 3 shall also apply to the income from immovable property of an enterprise.

Article 7
Business Profits

1. The profits of an enterprise of a Contracting State shall be taxable only in that State unless the enterprise carries on business in the other Contracting State through a permanent establishment situated therein. If the enterprise carries on business as aforesaid, the profits of the enterprise may be taxed in the other State but only so much of them as is attributable to that permanent establishment.

2. Subject to the provisions of paragraph 3, where an enterprise of a Contracting State carries on business in the other Contracting State through a

permanent establishment situated therein, there shall in each Contracting State be attributed to that permanent establishment the profits which it might be expected to make if it were a distinct and separate enterprise engaged in the same or similar activities under the same or similar conditions and dealing wholly independently with the enterprise of which it is a permanent establishment.

3. In determining the profits of a permanent establishment, there shall be allowed as deductions expenses which are incurred for the purposes of the permanent establishment, including executive and general administrative expenses so incurred, whether in the State in which the permanent establishment is situated or elsewhere.

4. Insofar as it has been customary in a Contracting State to determine the profits to be attributed to a permanent establishment on the basis of an apportionment of the total profits of the enterprise to its various parts, nothing in paragraph 2 shall preclude that Contracting State from determining the profits to be taxed by such an apportionment as may be customary; the method of apportionment adopted shall, however, be such that the result shall be in accordance with the principles contained in this Article.

5. No profits shall be attributed to a permanent establishment by reason of the mere purchase by that permanent establishment of goods or merchandise for the enterprise.

6. For the purposes of the preceding paragraphs, the profits to be attributed to the permanent establishment shall be determined by the same method year by year unless there is good and sufficient reason to the contrary.

7. Where profits include items of income which are dealt with separately in other Articles of this Convention, then the provisions of those Articles shall not be affected by the provisions of this Article.

Article 8
Shipping, Inland Waterways Transport and Air Transport

1. Profits from the operation of ships or aircraft in international traffic shall be taxable only in the Contracting State in which the place of effective management of the enterprise is situated.

2. Profits from the operation of boats engaged in inland waterways transport shall be taxable only in the Contracting State in which the place of effective management of the enterprise is situated.

3. If the place of effective management of a shipping enterprise or of an inland waterways transport enterprise is aboard a ship or boat, then it shall be deemed to be situated in the Contracting State in which the home harbour of the ship or boat is situated, or, if there is no such home harbour, in the Contracting State of which the operator of the ship or boat is a resident.

4. The provisions of paragraph 1 shall also apply to profits from the participation in a pool, a joint business or an international operating agency.

Article 9
Associated Enterprises

1. Where

a) an enterprise of a Contracting State participates directly or indirectly in the management, control or capital of an enterprise of the other Contracting State, or

b) the same persons participate directly or indirectly in the management, control or capital of an enterprise of a Contracting State and an enterprise of the other Contracting State, and in either case conditions are made or imposed between the two enterprises in their commercial or financial relations which differ from those which would be made between independent enterprises, then any profits which would, but for those conditions, have accrued to one of the enterprises, but, by reason of those conditions, have not so accrued, may be included in the profits of that enterprise and taxed accordingly.

2. Where a Contracting State includes in the profits of an enterprise of that State — and taxes accordingly — profits on which an enterprise of the other Contracting State has been charged to tax in that other State and the profits so included are profits which would have accrued to the enterprise of the first-mentioned State if the conditions made between the two enterprises had been those which would have been made between independent enterprises, then that other State shall make an appropriate adjustment to the amount of the tax charged therein on those profits. In determining such adjustment, due regard shall be had to the other provisions of this Convention and the competent authorities of the Contracting States shall if necessary consult each other.

Article 10
Dividends

1. Dividends paid by a company which is a resident of a Contracting State to a resident of the other Contracting State may be taxed in that other State.

2. However, such dividends may also be taxed in the Contracting State of which the company paying the dividends is a resident and according to the laws of that State, but if the beneficial owner of the dividends is a resident of the other Contracting State, the tax so charged shall not exceed: a) 5 per cent of the gross amount of the dividends if the beneficial owner is a company (other than a partnership) which holds directly

at least 25 per cent of the capital of the company paying the dividends; b) 15 per cent of the gross amount of the dividends in all other cases. The competent authorities of the Contracting States shall by mutual agreement settle the mode of application of these limitations. This paragraph shall not affect the taxation of the company in respect of the profits out of which the dividends are paid.

3. The term "dividends" as used in this Article means income from shares, "jouissance" shares or "jouissance" rights, mining shares, founders' shares or other rights, not being debt-claims, participating in profits, as well as income from other corporate rights which is subjected to the same taxation treatment as income from shares by the laws of the State of which the company making the distribution is a resident.

4. The provisions of paragraphs 1 and 2 shall not apply if the beneficial owner of the dividends, being a resident of a Contracting State, carries on business in the other Contracting State of which the company paying the dividends is a resident through a permanent establishment situated therein and the holding in respect of which the dividends are paid is effectively connected with such permanent establishment. In such case the provisions of Article 7 shall apply.

5. Where a company which is a resident of a Contracting State derives profits or income from the other Contracting State, that other State may not impose any tax on the dividends paid by the company, except insofar as such dividends are paid to a resident of that other State or insofar as the holding in respect of which the dividends are paid is effectively connected with a permanent establishment situated in that other State, nor subject the company's undistributed profits to a tax on the company's undistributed profits, even if the dividends paid or the undistributed profits consist wholly or partly of profits or income arising in such other State.

Article 11
Interest

1. Interest arising in a Contracting State and paid to a resident of the other Contracting State may be taxed in that other State.

2. However, such interest may also be taxed in the Contracting State in which it arises and according to the laws of that State, but if the beneficial owner of the interest is a resident of the other Contracting State, the tax so charged shall not exceed 10 per cent of the gross amount of the interest. The competent authorities of the Contracting States shall by mutual agreement settle the mode of application of this limitation.

3. The term "interest" as used in this Article means income from debt-claims of every kind, whether or not secured by mortgage and whether or not carrying a right to participate in the debtor's profits, and in particular, income from government securities and income from bonds or debentures, including premiums and prizes attaching to such securities, bonds or debentures. Penalty charges for late payment shall not be regarded as interest for the purpose of this Article.

4. The provisions of paragraphs 1 and 2 shall not apply if the beneficial owner of the interest, being a resident of a Contracting State, carries on business in the other Contracting State in which the interest arises through a permanent establishment situated therein and the debt-claim in respect of which the interest is paid is effectively connected with such permanent establishment. In such case the provisions of Article 7 shall apply.

5. Interest shall be deemed to arise in a Contracting State when the payer is a resident of that State. Where, however, the person paying the interest, whether he is a resident of a Contracting State or not, has in a Contracting State a permanent establishment in connection with which the indebtedness on which the interest is paid was incurred, and such interest is borne by such permanent establishment, then such interest shall be deemed to arise in the State in which the permanent establishment is situated.

6. Where, by reason of a special relationship between the payer and the beneficial owner or between both of them and some other person, the amount of the interest, having regard to the debt-claim for which it is paid, exceeds the amount which would have been agreed upon by the payer and the beneficial owner in the absence of such relationship, the provisions of this Article shall apply only to the last-mentioned amount. In such case, the excess part of the payments shall remain taxable according to the laws of each Contracting State, due regard being had to the other provisions of this Convention.

Article 12
Royalties

1. Royalties arising in a Contracting State and beneficially owned by a resident of the other Contracting State shall be taxable only in that other State.

2. The term "royalties" as used in this Article means payments of any kind received as a consideration for the use of, or the right to use, any copyright of literary, artistic or scientific work including cinematograph films, any patent, trade mark, design or model, plan, secret formula or process, or for information concerning industrial, commercial or scientific experience.

3. The provisions of paragraph 1 shall not apply if the beneficial owner of the royalties, being a resident of a Contracting State, carries on business in the other Contracting State in which the royalties arise through a permanent establishment situated therein and the right or property in respect of which the royalties are paid

is effectively connected with such permanent establishment. In such case the provisions of Article 7 shall apply.

4. Where, by reason of a special relationship between the payer and the beneficial owner or between both of them and some other person, the amount of the royalties, having regard to the use, right or information for which they are paid, exceeds the amount which would have been agreed upon by the payer and the beneficial owner in the absence of such relationship, the provisions of this Article shall apply only to the last-mentioned amount. In such case, the excess part of the payments shall remain taxable according to the laws of each Contracting State, due regard being had to the other provisions of this Convention.

Article 13
Capital Gains

1. Gains derived by a resident of a Contracting State from the alienation of immovable property referred to in Article 6 and situated in the other Contracting State may be taxed in that other State.

2. Gains from the alienation of movable property forming part of the business property of a permanent establishment which an enterprise of a Contracting State has in the other Contracting State, including such gains from the alienation of such a permanent establishment (alone or with the whole enterprise), may be taxed in that other State.

3. Gains from the alienation of ships or aircraft operated in international traffic, boats engaged in inland waterways transport or movable property pertaining to the operation of such ships, aircraft or boats, shall be taxable only in the Contracting State in which the place of effective management of the enterprise is situated.

4. Gains derived by a resident of a Contracting State from the alienation of shares deriving more than 50 per cent of their value directly or indirectly from immovable property situated in the other Contracting State may be taxed in that other State.

5. Gains from the alienation of any property, other than that referred to in paragraphs 1, 2, 3 and 4, shall be taxable only in the Contracting State of which the alienator is a resident

Article 14
Independent Personal Services [Deleted]

Article 15
Income From Employment

1. Subject to the provisions of Articles 16, 18 and 19, salaries, wages and other similar remuneration derived by a resident of a Contracting State in respect of an employment shall be taxable only in that State unless the employment is exercised in the other Contracting State. If the employment is so exercised, such remuneration as is derived therefrom may be taxed in that other State.

2. Notwithstanding the provisions of paragraph 1, remuneration derived by a resident of a Contracting State in respect of an employment exercised in the other Contracting State shall be taxable only in the first-mentioned State if: a) the recipient is present in the other State for a period or periods not exceeding in the aggregate 183 days in any twelve month period commencing or ending in the fiscal year concerned, and b) the remuneration is paid by, or on behalf of, an employer who is not a resident of the other State, and c) the remuneration is not borne by a permanent establishment which the employer has in the other State.

3. Notwithstanding the preceding provisions of this Article, remuneration derived in respect of an employment exercised aboard a ship or aircraft operated in international traffic, or aboard a boat engaged in inland waterways transport, may be taxed in the Contracting State in which the place of effective management of the enterprise is situated.

Article 16
Directors' Fees

Directors' fees and other similar payments derived by a resident of a Contracting State in his capacity as a member of the board of directors of a company which is a resident of the other Contracting State may be taxed in that other State.

Article 17
Artistes and Sportsmen

1. Notwithstanding the provisions of Articles 7 and 15, income derived by a resident of a Contracting State as an entertainer, such as a theatre, motion picture, radio or television artiste, or a musician, or as a sportsman, from his personal activities as such exercised in the other Contracting State, may be taxed in that other State.

2. Where income in respect of personal activities exercised by an entertainer or a sportsman in his capacity as such accrues not to the entertainer or sportsman himself but to another person, that income may, notwithstanding the provisions of Articles 7 and 15, be taxed in the Contracting State in which the activities of the entertainer or sportsman are exercised.

Article 18
Pensions

Subject to the provisions of paragraph 2 of Article 19, pensions and other similar remuneration paid to a resident of a Contracting State in consideration of past employment shall be taxable only in that State.

Article 19
Government Service

1.a) Salaries, wages and other similar remuneration, other than a pension, paid by a Contracting State or a political subdivision or a local authority thereof to an individual in respect of services rendered to that State or subdivision or authority shall be taxable only in that State. b) However, such salaries, wages and other similar remuneration shall be taxable only in the other Contracting State if the services are rendered in that State and the individual is a resident of that State who: (i) is a national of that State; or (ii) did not become a resident of that State solely for the purpose of rendering the services.

2. a) Any pension paid by, or out of funds created by, a Contracting State or a political subdivision or a local authority thereof to an individual in respect of services rendered to that State or subdivision or authority shall be taxable only in that State. b) However, such pension shall be taxable only in the other Contracting State if the individual is a resident of, and a national of, that State.

3. The provisions of Articles 15, 16, 17, and 18 shall apply to salaries, wages and other similar remuneration, and to pensions, in respect of services rendered in connection with a business carried on by a Contracting State or a political subdivision or a local authority thereof.

Article 20
Students

Payments which a student or business apprentice who is or was immediately before visiting a Contracting State a resident of the other Contracting State and who is present in the first-mentioned State solely for the purpose of his education or training receives for the purpose of his maintenance, education or training shall not be taxed in that State, provided that such payments arise from sources outside that State.

Article 21
Other Income

1. Items of income of a resident of a Contracting State, wherever arising, not dealt with in the foregoing Articles of this Convention shall be taxable only in that State.

2. The provisions of paragraph 1 shall not apply to income, other than income from immovable property as defined in paragraph 2 of Article 6, if the recipient of such income, being a resident of a Contracting State, carries on business in the other Contracting State through a permanent establishment situated therein and the right or property in respect of which the income is paid is effectively connected with such permanent establishment. In such case the provisions of Article 7 shall apply.

CHAPTER IV
Taxation of Capital

Article 22
Capital

1. Capital represented by immovable property referred to in Article 6, owned by a resident of a Contracting State and situated in the other Contracting State, may be taxed in that other State.

2. Capital represented by movable property forming part of the business property of a permanent establishment which an enterprise of a Contracting State has in the other Contracting State may be taxed in that other State.

3. Capital represented by ships and aircraft operated in international traffic and by boats engaged in inland waterways transport, and by movable property pertaining to the operation of such ships, aircraft and boats, shall be taxable only in the Contracting State in which the place of effective management of the enterprise is situated.

4. All other elements of capital of a resident of a Contracting State shall be taxable only in that State.

CHAPTER V

Methods for Elimination of Double Taxation

Article 23 A
Exemption Method

1. Where a resident of a Contracting State derives income or owns capital which, in accordance with the provisions of this Convention, may be taxed in the other Contracting State, the first-mentioned State shall, subject to the provisions of paragraphs 2 and 3, exempt such income or capital from tax.

2. Where a resident of a Contracting State derives items of income which, in accordance with the provisions of Articles 10 and 11, may be taxed in the other Contracting State, the first-mentioned State shall allow as a deduction from the tax on the income of that resident an amount equal to the tax paid in that other State. Such deduction shall not, however, exceed that part of the tax, as computed before the deduction is given, which is attributable to such items of income derived from that other State.

3. Where in accordance with any provision of the Convention income derived or capital owned by a resident of a Contracting State is exempt from tax in that State, such State may nevertheless, in calculating the amount of tax on the remaining income or capital of such resident, take into account the exempted income or capital.

4. The provisions of paragraph 1 shall not apply to income derived or capital owned by a resident of a Contracting State where the other Contracting State applies the provisions of the Convention to exempt such income or capital from tax or applies the provisions of paragraph 2 of Article 10 or 11 to such income.

Article 23 B
Credit Method

1. Where a resident of a Contracting State derives income or owns capital which, in accordance with the provisions of this Convention, may be taxed in the other Contracting State, the first-mentioned State shall allow: a) as a deduction from the tax on the income of that resident, an amount equal to the income tax paid in that other State; b) as a deduction from the tax on the capital of that resident, an amount equal to the capital tax paid in that other State. Such deduction in either case shall not, however, exceed that part of the income tax or capital tax, as computed before the deduction is given, which is attributable, as the case may be, to the income or the capital which may be taxed in that other State.

2. Where in accordance with any provision of the Convention income derived or capital owned by a resident of a Contracting State is exempt from tax in that State, such State may nevertheless, in calculating the amount of tax on the remaining income or capital of such resident, take into account the exempted income or capital.

CHAPTER VI
Special Provisions

Article 24
Non-Discrimination

1. Nationals of a Contracting State shall not be subjected in the other Contracting State to any taxation or any requirement connected therewith, which is other or more burdensome than the taxation and connected requirements to which nationals of that other State in the same circumstances, in particular with respect to residence, are or may be subjected. This provision shall, notwithstanding the provisions of Article 1, also apply to persons who are not residents of one or both of the Contracting States.

2. Stateless persons who are residents of a Contracting State shall not be subjected in either Contracting State to any taxation or any requirement connected therewith, which is other or more burdensome than the taxation and connected requirements to which nationals of the State concerned in the same circumstances, in particular with respect to residence, are or may be subjected.

3. The taxation on a permanent establishment which an enterprise of a Contracting State has in the other Contracting State shall not be less favourably levied in that other State than the taxation levied on enterprises of that other State carrying on the same activities. This provision shall not be construed as obliging a Contracting State to grant to residents of the other Contracting State any personal allowances, reliefs and reductions for taxation purposes on account of civil status or family responsibilities which it grants to its own residents.

4. Except where the provisions of paragraph 1 of Article 9, paragraph 6 of Article 11, or paragraph 4 of Article 12, apply, interest, royalties and other disbursements paid by an enterprise of a Contracting State to a resident of the other Contracting State shall, for the purpose of determining the taxable profits of such enterprise, be deductible under the same conditions as if they had been paid to a resident of the first-mentioned State. Similarly, any debts of an enterprise of a Contracting State to a resident of the other Contracting State shall, for the purpose of determining the taxable capital of such enterprise, be deductible under the same conditions as if they had been contracted to a resident of the first-mentioned State.

5. Enterprises of a Contracting State, the capital of which is wholly or partly owned or controlled, directly or indirectly, by one or more residents of the other Contracting State, shall not be subjected in the first-mentioned State to any taxation or any requirement connected therewith which is other or more burdensome than the taxation and connected requirements to which other similar enterprises of the first-mentioned State are or may be subjected.

6. The provisions of this Article shall, notwithstanding the provisions of Article 2, apply to taxes of every kind and description.

Article 25
Mutual Agreement Procedure

1. Where a person considers that the actions of one or both of the Contracting States result or will result for him in taxation not in accordance with the provisions of this Convention, he may, irrespective of the remedies provided by the domestic law of those States, present his case to the competent authority of the Contracting State of which he is a resident or, if his case comes under paragraph 1 of Article 24, to that of the Contracting State of which he is a national. The case must be presented within three years from the first notification of the action resulting in taxation not in accordance with the provisions of the Convention.

2. The competent authority shall endeavour, if the objection appears to it to be justified and if it is not itself able to arrive at a satisfactory solution, to resolve the

case by mutual agreement with the competent authority of the other Contracting State, with a view to the avoidance of taxation which is not in accordance with the Convention. Any agreement reached shall be implemented notwithstanding any time limits in the domestic law of the Contracting States.

3. The competent authorities of the Contracting States shall endeavour to resolve by mutual agreement any difficulties or doubts arising as to the interpretation or application of the Convention. They may also consult together for the elimination of double taxation in cases not provided for in the Convention.

4. The competent authorities of the Contracting States may communicate with each other directly, including through a joint commission consisting of themselves or their representatives, for the purpose of reaching an agreement in the sense of the preceding paragraphs.

Article 26
Exchange of Information

1. The competent authorities of the Contracting States shall exchange such information as is necessary for carrying out the provisions of this Convention or of the domestic laws concerning taxes of every kind and description imposed on behalf of the Contracting States, or of their political subdivisions or local authorities, insofar as the taxation thereunder is not contrary to the Convention. The exchange of information is not restricted by Articles 1 and 2. Any information received by a Contracting State shall be treated as secret in the same manner as information obtained under the domestic laws of that State and shall be disclosed only to persons or authorities (including courts and administrative bodies) concerned with the assessment or collection of, the enforcement or prosecution in respect of, or the determination of appeals in relation to the taxes referred to in the first sentence. Such persons or authorities shall use the information only for such purposes. They may disclose the information in public court proceedings or in judicial decisions.

2. In no case shall the provisions of paragraph 1 be construed so as to impose on a Contracting State the obligation: a) to carry out administrative measures at variance with the laws and administrative practice of that or of the other Contracting State; b) to supply information which is not obtainable under the laws or in the normal course of the administration of that or of the other Contracting State; c) to supply information which would disclose any trade, business, industrial, commercial or professional secret or trade process, or information, the disclosure of which would be contrary to public policy (order public).

Article 27
Assistance in the Collection of Taxes

1. The Contracting States shall lend assistance to each other in the collection of revenue claims. This assistance is not restricted by Articles 1 and 2. The competent authorities of the Contracting States may by mutual agreement settle the mode of application of this Article.

2. The term "revenue claim" as used in this Article means an amount owed in respect of taxes of every kind and description imposed on behalf of the Contracting States, or of their political subdivisions or local authorities, insofar as the taxation thereunder is not contrary to this Convention or any other instrument to which the Contracting States are parties, as well as interest, administrative penalties and costs of collection or conservancy related to such amount.

3. When a revenue claim of a Contracting State is enforceable under the laws of that State and is owed by a person who, at that time, cannot, under the laws of that State, prevent its collection, that revenue claim shall, at the request of the competent authority of that State, be accepted for purposes of collection by the competent authority of the other Contracting State. That revenue claim shall be collected by that other State in accordance with the provisions of its laws applicable to the enforcement and collection of its own taxes as if the revenue claim were a revenue claim of that other State.

4. When a revenue claim of a Contracting State is a claim in respect of which that State may, under its law, take measures of conservancy with a view to ensure its collection, that revenue claim shall, at the request of the competent authority of that State, be accepted for purposes of taking measures of conservancy by the competent authority of the other Contracting State. That other State shall take measures of conservancy in respect of that revenue claim in accordance with the provisions of its laws as if the revenue claim were a revenue claim of that other State even if, at the time when such measures are applied, the revenue claim is not enforceable in the first mentioned State or is owed by a person who has a right to prevent its collection.

5. Notwithstanding the provisions of paragraphs 3 and 4, a revenue claim accepted by a Contracting State for purposes of paragraph 3 or 4 shall not, in that State, be subject to the time limits or accorded any priority applicable to a revenue claim under the laws of that State by reason of its nature as such. In addition, a revenue claim accepted by a Contracting State for the purposes of paragraph 3 or 4 shall not, in that State, have any priority applicable to that revenue claim under the laws of the other Contracting State.

6. Proceedings with respect to the existence, validity or the amount of a revenue claim of a

Contracting State shall not be brought before the courts or administrative bodies of the other Contracting State.

7. Where, at any time after a request has been made by a Contracting State under paragraph 3 or 4 and before the other Contracting State has collected and remitted the relevant revenue claim to the first-mentioned State, the relevant revenue claim ceases to be a) in the case of a request under paragraph 3, a revenue claim of the first-mentioned State that is enforceable under the laws of that State and is owed by a person who, at that time, cannot, under the laws of that State, prevent its collection, or b) in the case of a request under paragraph 4, a revenue claim of the first-mentioned State in respect of which that State may, under its laws, take measures of conservancy with a view to ensure its collection the competent authority of the first-mentioned State shall promptly notify the competent authority of the other State of that fact and, at the option of the other State, the first mentioned State shall either suspend or withdraw its request.

8. In no case shall the provisions of this Article be construed so as to impose on a Contracting State the obligation: a) to carry out administrative measures at variance with the laws and administrative practice of that or of the other Contracting State; b) to carry out measures which would be contrary to public policy (order public); c) to provide assistance if the other Contracting State has not pursued all reasonable measures of collection or conservancy, as the case may be, available under its laws or administrative practice; d) to provide assistance in those cases where the administrative burden for that State is clearly disproportionate to the benefit to be derived by the other Contracting State.

Article 28
Members of Diplomatic Missions and Consular Posts

Nothing in this Convention shall affect the fiscal privileges of members of diplomatic missions or consular posts under the general rules of international law or under the provisions of special agreements.

Article 29
Territorial Extension

1. This Convention may be extended, either in its entirety or with any necessary modifications [to any part of the territory of (State A) or of (State B) which is specifically excluded from the application of the Convention or], to any State or territory for whose international relations (State A) or (State B) is responsible, which imposes taxes substantially similar in character to those to which the Convention applies. Any such extension shall take effect from such date and subject to such modifications and conditions, including conditions as to termination, as may be specified and agreed between the Contracting States in notes to be exchanged through diplomatic channels or in any other manner in accordance with their constitutional procedures.

2. Unless otherwise agreed by both Contracting States, the termination of the Convention by one of them under Article 30 shall also terminate, in the manner provided for in that Article, the application of the Convention [to any part of the territory of (State A) or of (State B) or] to any State or territory to which it has been extended under this Article.

CHAPTER VII
Final Provisions

Article 30
Entry Into Force

1. This Convention shall be ratified and the instruments of ratification shall be exchanged at .... as soon as possible.

2. The Convention shall enter into force upon the exchange of instruments of ratification and its provisions shall have effect:

a) (in State A): ....

b) (in State B): ....

Article 31
Termination

This Convention shall remain in force until terminated by a Contracting State. Either Contracting State may terminate the Convention, through diplomatic channels, by giving notice of termination at least six months before the end of any calendar year after the year ...... In such event, the Convention shall cease to have effect:

a) (in State A): ....
b) (in State B): ....

Terminal Clause

Tax Treaty and Municipal Law. - Treaties are in the nature of international agreements which need Senate ratification. Municipal legislations are local laws passed by the legislature governing internal matters. It is not uncommon that international agreements and local legislation conflict with each other.

Finally, in case of conflict between the Constitution (municipal law) and treaty provisions, the former shall prevail. Of course, an interpretation that would give effect to both shall first be resorted to.

"Our abiding concern throughout these proceedings is to extend the most relief to our people, balancing this with the government's ambitious vision of jump-starting our country's economic growth. At the end of the day, our main aim is to help as many Filipino families as we can within fiscal limits and to enact reforms that allow them to take home more from their hard work.

"Kaya ang dapat sagutin po natin ngayon ay, makakatulong po ba tayo sa pamilyang Pilipino kapag ipinasa po natin ang ating panukalang reporma na dinidinig ngayon? Pinapababaan po natin ang income tax, nakakasiguro po tayo na kakayanin ng karaniwang tao ang dagdag na buwis o ang kaakibat nitong pagtaas sa presyo ng mga bilihin. Susuriin po natin ang mga pangangatwiran at lahat po ng presentasyon, lahat po mabibigyan ng pagkakataon para magbigay ng kanila opinion dito sa mga usapin natin.

"A wise and successful politician once said in 1985, *"The worth of any economic policy must be measured by the strength of its commitment to families, the bedrock of society. There is no instrument of hard work, savings and job creation as effective as the family. There is no cultural institution as ennobling as family life. And there is no superior, indeed no equal, means to rear the young, protect the weak, or attend to the elderly." So pamilya po dapat sana ang sentro ng ating usapin ngayon, although many of you represent corporations, at the end of the day, we all have families. So I think they must be at the center of our discussion"*.

[Opening Statement of Senator Sonny Angara during the January 31, 2017 Public Hearing on the Revised Department of Finance (DOF) Tax Reform Program].

* Prepared by: Mr. Clinton S. Martinez, SLSO II, ODG

TAX NEWS DIGEST

"*Local stocks seen starting 2017 on sluggish note*"

"After a long holiday break, the local stock market is seen to reopen today still on a sluggish note.

"For the full year 2016, the Philippine Stock Exchange index lost 1.6 percent to close at 6,840.64, marking the second straight year of decline for the local stock barometer.

"I think that in the first few days of January, it will still be a little bit down," said AsiaSec Equities chief strategist Manny Cruz, "But market has strong support at 6,700."

"Cruz said it was possible that the PSEi would retest 7,000 within this month.

"The positive development we've seen before yearend close was that we seem to have a buying momentum for foreign investors," Cruz said, noting the net foreign buying in the last two trading days of 2016, "Hopefully, the momentum will be sustained." (PDI, 3 January 2017)

"*Tetangco: Ph economy ready to take on 2017*"

"Despite heightened global uncertainties seen this year, the Philippines' sound macro fundamentals would shield the domestic economy as the Bangko Sentral ng Pilipinas continues to implement additional reforms to further strengthen the banking system, Governor Armando M. Tetangco Jr. said.

"In an e-mail to the Inquirer, Tetangco believes 2017 would be a trying year.

"There are many moving parts in the global environment that are subject to great uncertainty and thus really difficult to predict. Political developments in many countries may spell significant shifts in policies that could have enormous effect on the world economy. Of late, global markets have tended to react to every piece of news more intensely, resulting in overshooting in certain cases. This kind of environment makes policy formulation greatly challenging and policy transmission more complicated." (PDI, 3 January 2017)

By: Mr. Clinton S. Martinez, SLSO II

"BOI '16 investment pledges up 20%"

"The total value of investment pledges approved by the Board of Investments (BOI) last year rose 20 percent to P441.8 billion, the second highest level since 2000.

"The growth in registered investments last year also far exceeded the agency's target of just 7 percent.

"According to Trade Secretary and BOI chair Ramon M. Lopez, the growth last year was driven by the continued investor confidence in the country's sustained strong macroeconomic fundamentals and President Duterte's 10-point socioeconomic agenda as well as state visits.

"With the investment missions that we are doing, investors have gained greater awareness of the Philippines' strong and growing economy," Lopez said.

"Data from the BOI showed that the investments approved in 2016 were for 377 projects that could generate about 67,615 new jobs once these become fully operational.

"Of the pledges approved last year, the bulk or P209.9 billion are to be allocated for energy projects; P65.8 billion for real estate activities; P62.3 billion for construction; P49 billion for manufacturing; and P23.4 billion for transportation and storage." (PDI, 3 January 2017)

"Gov't agencies given up to end of Q1 to submit 2018 budget proposal"

"The Department of Budget and Management has ordered government agencies to submit their respective budget proposals for 2018 on or before March 31, as the government intends to sustain the timely submission to Congress of the planned P3.84-trillion national budget.

"In National Budget Memorandum No. 127 containing the budget call for fiscal year 2018, Budget Secretary Benjamin E. Diokno said details of the agencies' approved budget ceilings and new spending proposals for next year must be submitted by the end of the first quarter.

"For 2018, the government will pitch a record P3.84-trillion national budget, up 14.6 percent from the P3.35-trillion budget for this year, the Cabinet-level, interagency Development Budget Coordination Committee (DBCC) said in a report.

"The proposed 2018 budget will represent 21.6 percent of the gross domestic product (GDP), according to the DBCC.

"In the memorandum, Diokno said the 2018 budget proposal must "sustain the President's zero plus 10-point socioeconomic agenda."

"Including the "zero" in the 10-point agenda which is peace and order, the Duterte administration's development blueprint was aimed at reducing poverty incidence to about 14 percent by 2022 from 21.6 percent last year.

"Diokno said the 2018 budget should also "strengthen multi-year focus of the budget, including the acceleration of infrastructure spending from 5 percent of GDP." (PDI, 4 January 2017)

"PH business optimism slides. Still higher than levels in Asia-Pacific peers"

"Business leaders across Asia Pacific are divided over the region's economic prospects as 2017 dawns, indicating that emerging and developed nations are taking diverging tracks, according to the latest quarterly survey of audit and consulting firm Grant Thornton.

"Research from the firm's International Business Report shows that business optimism among developed Asia-Pacific economies fell 8 percentage points in the fourth quarter of 2016 to net -16 percent.

"Japan fell 8 percentage points to -45 percent. Among emerging economies in the region, the picture is much brighter. Business optimism rose 11 percentage points to 53 percent.

"Yet, the Philippines has been seeing a decline in optimism in 2016," it said in a statement. "Starting with

only 56 percent in the first quarter, the country saw an unprecedented rise in the second quarter to 94 percent. However, the Philippines experienced a sudden drop of 10 percentage points in the third quarter, which has continued to descend to 80 percent in the fourth quarter."

"Globally, business optimism at the end of the fourth quarter of 2016 stands at net 38 percent, up 5 percentage points from the previous quarter and the highest since the third quarter of 2015.

"The global survey was conducted among 2,600 businesses in 37 economies, it said." (PDI, 4 January 2017)

"*New corporate governance code out*"

"The Securities and Exchange Commission has issued a new corporate governance code for publicly listed companies that includes rules setting a nine-year term limit for independent directors, mandates protection for whistle-blowers and incorporates anticorruption measures.

"The code revision is part of the SEC's partnership with International Finance Corp. (IFC) and is aimed at enhancing the country's regulatory framework and investment climate.

"The new code—which took effect on Jan. 1, 2017—aims to improve the functioning of boards, strengthen shareholder protection and promote full disclosure in financial and non-financial reporting.

"All publicly listed companies are required to submit a new Manual on Corporate Governance to the SEC on or before May 31, 2017.

"By providing guidance to adopt best governance practices, Philippine publicly listed companies are seen to improve their competitiveness and ability to attract foreign investment.

"The new code will increase the responsibilities of the board and ensure the competence and commitment of its directors. It adopts a "comply or explain" approach that combines voluntary compliance with mandatory disclosure." (PDI, 5 January 2017)

"*First BSP deposit facility auction in '17 oversubscribed*"

"Banks swarmed the Bangko Sentral ng Pilipinas' 2017's first term deposit facility (TDF) auction Wednesday following several undersubscribed auctions last December.

"For the P30 billion in seven-day term deposits offered by the BSP, P43.991 billion were tendered.

"The BSP fully awarded all the one-week facility at a yield of 3-3.1 percent.

"For the P150 billion in 28-day TDF, bids reached P217.523 billion.

"The yield for the one-month term deposit was within the 3-3.495 percent range.

"On Jan. 11 and 18, the BSP will offer a total of P180 billion in its TDF auctions—P30 billion in seven-day and P150 billion in 28-day facility.

"At the last auction for 2016, tenders for one-month term deposits offered by the Bangko Sentral ng Pilipinas were undersubscribed.

"BSP officials said they expected the undersubscription during the holiday season, as banks would hold on to their cash to serve high seasonal demand.

"According to BSP Governor Amando M. Tetancgo Jr., the bids they rejected last Dec. 28 "were outside the interest rate corridor."

"As to the offered amount, the BSP continues to monitor the level of liquidity in the system and has the flexibility to change the volume it will offer for the TDF depending on the needs of the financial system," Tetangco said." (PDI, 5 January 2017)

CARGILL PHILIPPINES, INC., *Petitioner*, *v.* COMMISSIONER OF INTERNAL REVENUE, *Respondent*, G.R. No. 203774, March 11, 2015 (PERLAS-BERNABE, *J)*

Facts:

This case involves the legality of the tax refund filed by Cargill Philippines, Inc. (Cargill) with the Bureau of Internal Revenue (BIR) / Commissioner of Internal Revenue (CIR).

Cargill is a value-added tax (VAT)-registered domestic corporation, duly organized and existing under Philippine laws. Its primary purpose is to own, operate, run, and manage plants and facilities for the production, crushing, extracting, or otherwise manufacturing and refining of coconut oil, coconut meal, vegetable oil, lard, margarine, edible oil, and other articles of similar nature and their by-products. Petitioner alleged that it made overpayments in its VAT on the ground that the same were due to its export sales of coconut oil, the proceeds of which were paid for in acceptable foreign currency and accounted for in accordance with the rules and regulations of the Bangko Sentral ng Pilipinas (BSP) and, hence, are zero-rated for VAT purposes.

Petitioner filed both administrative (BIR) and judicial (Court of Tax Appeals [CTA]) claims for refund. The CIR asserts that the claims were not properly documented and denied the same. The case reached the CTA.

The CTA Division ruled that the 120-day period provided under Section 112(D) of the National Internal Revenue Code (NIRC) must be observed prior to the filing of a judicial claim for tax refund. As Cargill failed to comply therewith, the CTA Division, without ruling on the merits, dismissed the consolidated cases for being prematurely filed.

The CTA En Banc affirmed the Division ruling stating that Cargill's premature filing of its claims divested the CTA of jurisdiction, and warranted the dismissal of its petitions. It stressed that its petition in CTA Case No. 6714 was filed on June 30, 2003, or after the lapse of three (3) days from the time it filed its administrative claim with the BIR; while its petition in CTA Case No. 7672 was filed on the same date it filed its administrative claim with the BIR, *i.e.*, on May 31, 2005. Hence, the CTA *En Banc* ruled that Cargill's judicial claims were correctly dismissed for being filed prematurely.

Issue/s:

Whether or not the CTA En Banc correctly affirmed the CTA Division's dismissal of Cargill's claims for refund of unutilized input VAT on the ground of prematurity.

Ruling:

The Supreme Court (SC) held that the petition is partly meritorious. The SC affirmed the CTA En Banc decision in Case No. 779. Upon the other hand, Case No. 7262 was reinstated and remanded to the CTA Special First Division for resolution on the merits.

By: Mr. Clinton S. Martinez, SLSO II

The SC harmonized two previous decisions in the cases of *Aichi* and *San Roque* stating that:

"Reconciling the pronouncements in the Aichi and San Roque cases, the rule must therefore be that during the period December 10, 2003 (when BIR Ruling No. DA-489-03 was issued) to October 6, 2010 when the Aichi case was promulgated), taxpayers-claimants need not observe the 120-day period before it could file a judicial claim for refund of excess input VAT before the CTA. Before and after the aforementioned period (i.e., December 10, 2003 to October 6, 2010), the observance of the 120-day period is mandatory and jurisdictional to the filing of such claim."

In resolving the issues involved, the SC made the ensuing pronouncements:

"In this case, records disclose that anent Cargill's first refund claim, it filed its administrative claim with the BIR on June 27, 2003, and its judicial claim before the CTA on June 30, 2003, or before the period when BIR Ruling No. DA-489-03 was in effect, i.e., from December 10, 2003 to October 6, 2010. As such, it was incumbent upon Cargill to wait for the lapse of the 120-day period before seeking relief with the CTA, and considering that its judicial claim was filed only after three (3) days later, the CTA En Banc, thus, correctly dismissed Cargill's petition in CTA Case No. 6714 for being prematurely filed.

"In contrast, records show that with respect to Cargill's second refund claim, its administrative and judicial claims were both filed on May 31, 2005, or during the period of effectivity of BIR Ruling NO. DA-489-03, and, thus, fell within the exemption window period contemplated in San Roque, i.e., when taxpayer-claimants need not wait for the expiration of the 120-day period before seeking judicial relief. Verily, the CTA En Banc erred when it outrightly dismissed CTA Case No. 7262on the ground of prematurity.

"This notwithstanding, the Court finds that Cargill's second refund claim in the amount of P22,194,446.67 which allegedly represented unutilized input VAT covering the period March 1, 2003 to August 31, 2004 should not be instantly granted. This is because the determination of Cargill's entitlement to such claim, if any, would necessarily involve factual issues and, thus, are evidentiary in nature which are beyond the pale of judicial review under a Rule 45 petition where only pure questions of law, not of fact, may be resolved. Accordingly, the prudent course of action is to remand CTA Case No. 7262 to the CTA Division for resolution on the merits, consistent with the Court's ruling in Panay Power Corporation v. CIR."

EASTERN TELECOMMUNICATIONS PHILIPPINES, INC., *Petitioner*, *v.* COMMISSIONER OF INTERNAL REVENUE, *Respondent*, G.R. No. 183531, March 25, 2015 (REYES, *J)*

Facts:

Petitioner Eastern Telecommunications Philippines, Inc (ETPI) is a domestic corporation registered with the Bureau of Internal Revenue (BIR) as a VAT taxpayer.

As a telecommunications company, it entered into several international service agreements (ISAs) with international telecommunications carriers and handles incoming telecommunications services for non-resident foreign telecommunication companies and the relay of said international calls within and around other places in the Philippines. To broaden its distribution coverage throughout the country, ETPI entered into various interconnection agreements with local carriers that can relay the foreign calls to the intended local end-receiver. The foreign companies pay ETPI in US dollars remitted via local banks based on established international standards.

Petitioner seasonably filed its Quarterly VAT Returns for the year 1998 which it simultaneously amended on February 22, 2001 to correct its input VAT on domestic purchases of goods and services and on importation of goods and to reflect its zero-rated and exempt sales for said year.

On January 25, 2000, it filed an administrative claim for refund with the Bureau of Internal Revenue (BIR) representing excess input tax attributable to its effectively zero-rated sales in 1998 pursuant to Section 112 of the Republic Act (R.A.) No. 8424, Tax Code, as implemented by Revenue Regulations (RR) No. 5-87 and as amended by RR No. 7-95.

While the same was pending review by the BIR, Petitioner filed a Petition for Review before the Court of Tax Appeals (CTA) on February 21, 2000 in order to toll the two-year reglementary period under Section 229 of the Tax Code. The case was docketed as C.T.A. Case No. 6019. The Commissioner of Internal Revenue (CIR) opposed the petition and stated that the same cannot be instituted unless a claim has been duly filed before it. The BIR stressed that ETPI did not file a formal/written claim for refund but merely submitted a quarterly VAT return for the 4th quarter of

1998 contrary to what Section 229 of the NIRC prescribes.

The CTA petition because the VAT official receipts presented to support its claim, failed to imprint the word "*zero-rated*" on its face in violation of the invoicing requirements under Section 4.108-1 of RR No. 7-95.

The Tax Court said that even if ETPI is entitled to a refund, it still failed to present sales invoices covering those subject to VAT and exempt sales for purposes of allocating its input taxes. The CTA chastised Petitioner for filing its 1998 audited financial records on February 22, 2001 when the same should have been reported to the BIR as early as February 22, 1999. The CTA opined that tax refunds, being in the nature of tax exemptions, are construed in*strictissimi juris*against the taxpayer. Hence, ETPI's non-compliance with laws and regulations resulted to the denial of its claim for refund.

Issue/s:

Whether or not the Court of Tax Appeals erred in denying Eastern Telecommunications Philippines, Inc.'s claim for refund of input taxes resulting from its zero-rated sales.

Ruling:

The High Court stressed that the petition is bereft of merit. It underscored that the words "zero-rated" must be imprinted on the face of the invoice for a taxpayer to be able to claim a refund. Said the SC:

> "*In this respect, the Court has consistently ruled on the denial of a claim for refund or tax credit whenever the word "zero-rated" has been omitted on the invoices or sale receipts of the taxpayer-claimant as pronounced in Panasonic Communications Imaging Corporation of the Philippines v. CIR wherein it was ratiocinated, viz:*
>
> *"Section 4.108-1 of RR 7-95 proceeds from the rule-making authority granted to the Secretary of Finance under Section 245 of the 1977 NIRC (Presidential Decree 1158) for the efficient enforcement of the tax code and of course its amendments. The requirement is reasonable and is in accord with the efficient collection of VAT from the covered sales of goods and services. As aptly explained by the CTA's First Division, the appearance of the word "zero-rated" on the face of invoices covering zero-rated sales prevents buyers from falsely claiming input VAT from their purchases when no VAT was actually paid. If, absent such word, a successful claim for input VAT is made, the government would be refunding money it did not collect.*
>
> *"Further, the printing of the word "zero-rated" on the invoice helps segregate sales that are subject to 10% (now 12%) VAT from those sales that are zero-rated. Unable to submit the proper invoices, petitioner Panasonic has been unable to substantiate its claim for refund."*

Furthermore, the SC said that ETPI failed to substantiate its claim for tax refund or tax credit. The pronouncement stated:

> *"ETPI failed to discharge its burden to prove its claim. Tax refunds, being in the nature of tax exemptions, are construed in strictissimi juris against the taxpayer and liberally in favor of the government. Accordingly, it is a claimant's burden to prove the factual basis of a claim for refund or tax credit. Considering that ETPI is engaged in mixed transactions that cover its zero-rated sales, taxable and exempt sales, it is only appropriate and reasonable for it to present competent evidence to validate all entries in its returns in order to properly determine which transactions are zero-rated and which are taxable. Clearly, compliance with all the VAT invoicing requirements provided by tax laws and regulations is mandatory. A claim for unutilized input taxes attributable to zero-rated sales will be given due course; otherwise, the claim should be struck off for failure to do so, such as what ETPI did in the present case.*"

Finally, the High Tribunal mentioned that:

> *"ETPI failed to sufficiently substantiate the existence of its effectively zero-rated sales for taxable year 1998. It is noteworthy to state that the CTA is a highly specialized court dedicated exclusively to the study and consideration of revenue-related problems, in which it has necessarily developed an expertise. Hence, its factual findings, when supported by substantial evidence, will not be disturbed on appeal. Verily, this Court finds no sufficient reason to rule otherwise."*

The SC affirmed the Decision and Resolution of the CTA En Banc.

Atty. Rodelio T. Dascil

Plenary Speaker

Sharing his knowledge, expertise and insights on the Customs Modernization and Tariff Act (CMTA) and his practical knowledge of the customs law and its procedures before 1,200 customs administration students during the 8th Philippine Society of Customs Administration Students (PCAS) National Convention. held at the Filinvest Tent, Alabang, Muntinlupa City, on January 26, 2017.

Committee on Ways and Means chaired by Sen. Sonny Angara conducted a public hearing on Tax Reform for Acceleration and Inclusion, and heard all Stakeholders and solicited their inputs.

Senate of the Philippines, Recto Room
January 31, 2017

(From Right to left : Sen. Win Gatchalian, Sen. JV Ejercito, Sen. Sonny Angara, Sen. Nancy Binay, Sen. Migz Zubiri and DG-STSRO Atty. Rodelio T. Dascil)

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Website : http://www.senate.gov.ph
Email : stsro1989@gmail.com
Facebook : https://www.facebook.com/stsro.stsro
Telefax No. : 552-6850; Local 5506, 5508

Editors and Contributing Writers

Atty. RODELIO T. DASCIL, MNSA
Director General

RECHILDA B. GASCON, MNSA
Director III, Tax Policy & Admin

MARIA LUCRECIA R. MIR, PhD DA, MNSA
Director III, Direct Taxes

VIVIAN A. CABILING
Director III, Indirect Taxes

NORBERTO M. VILLANUEVA
Director II, Tax Policy & Admin

ELVIRA P. CRUDO
Director II, Direct Taxes

Atty. SHERRY ANNE C. SALAZAR
Director II, Indirect Taxes

CLINTON S. MARTINEZ
SLSO II, ODG

BONIFACIO R. JOSON
LSA-III, ODG - Layout Artist

The Articles were principally prepared by the authors, under the supervision of STSRO Directors and the overall guidance of its Director-General.

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