TAX MANAGEMENT ASSOCIATION OF THE PHILIPPINES, INC.

TAX UPDATES FOR DECEMBER 2014

Prepared by SGV & CO.

BIR Ruling

BIR Ruling No. 475-2014 dated November 26, 2014

A JV for construction is not taxable as a corporation if it complies with the conditions prescribed under RR No. 10-2012.

Facts:

A Co. and B Co. are both domestic corporations engaged in the construction business and are both licensed by the Philippine Contractors Accreditation Board (PCAB). A Co. and B Co. formed an unincorporated JV, also licensed by the PCAB, for a construction project. As co-venturers, A Co. and B Co. agreed to contribute all the necessary resources for the proper implementation of the project, and to share in the JV's profits and losses.

Issues:

1. Is the JV subject to corporate income tax?
2. Are the co-venturers subject to corporate income tax?
3. Are there other administrative requirements on the part of the co-venturers?

Ruling:

1. No. Under Section 22(B) of the Tax Code, the term "corporation" shall include partnerships, no matter how created or organized, but does not include JVs formed for the purpose of undertaking construction projects. This was implemented by RR No. 10-2012 which prescribes certain conditions which must be met for the non-taxability of a JV, thus:

   i. the JV is for the undertaking of a construction project,
   ii. the JV should involve joining or pooling of resources by PCAB-licensed local contractors,
   iii. the local contractors are engaged in the construction business, and
   iv. the JV itself is also registered with the PCAB.

   Since the JV between A Co. and B Co. complies with all these requirements, the JV between A Co. and B Co. is not subject to income tax as a corporation; consequently, income payments to it are not subject to the 2% creditable withholding tax (CWT).

2. Yes. The co-venturers are separately subject to the regular corporate income tax under Section 27(A) of the Tax Code on their taxable income during each taxable year respectively derived by them from the JV. The respective net income of the co-venturers derived from the JV is also subject to CWT under Section 57 of the Tax Code. Before the JV distributes the net income of the co-venturers, it shall withhold the tax due on such net income.

3. Yes. The co-venturers are required to enroll themselves to the BIR's Electronic Filing and Payment System (eFPS). The enrollment should be done at the Revenue District Office (RDO) where they are registered as taxpayers.

BIR Issuances

Revenue Regulations No. 10-2014 dated December 10, 2014

RR No. 10-2014 further amends Section 3 of RR No. 9-2001 and expands the coverage of taxpayers required to file returns and pay taxes through the eFPS.

► Definitions:

1. Taxpayer Account Management Program (TAMP) – Taxpayers, whether individual or juridical entities, that have been identified by RDO based on selection criteria pursuant to existing revenue issuances.

2. Accredited Importers with BIR Importer Clearance Certificates (ICCs) and Broker Clearance Certificates (BCCs) – All importers and customs brokers [individuals, partnerships, corporations, cooperatives, associations (whether taxable or non-taxable)], unless otherwise exempted, who secured accreditation from the BIR following existing revenue issuances, including prospective importers required to secure BIR-ICC and BIR-BCC.

► It is now mandatory for TAMP taxpayers and accredited importers, including prospective importers required to secure the ICC and BCCs, to make use of the eFPS facility in filing their returns and making tax payments.

► These Regulations shall take effect on all returns to be filed by the newly covered taxpayers to use the eFPS facility on January 1, 2015 or after 15 days following publication in a newspaper of general circulation, whichever comes later.

(Editor's Note: RR No. 10-2014 was published in the Manila Bulletin *on December 11, 2014.)*

Revenue Regulations No. 11-2014 dated December 5, 2014

RR No. 11-2014 further amends Section 2.57.2 of RR No. 2-98 on income payments subject to CWT, and lifts the suspension of the implementation of the CWT on locally produced raw sugar.

► The pertinent provisions of Section 2.57.2 of Revenue Regulations No. 2-98, as amended, are hereby further amended as follows:

> "*Income payments subject to creditable withholding tax and rates prescribed thereon*. – Except as herein otherwise provided, there shall be withheld a creditable income tax at the rates herein specified for each class of payee from the following items of income payments to persons residing in the Philippines:
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> XXX XXX XXX
>
> (M) *Income payment made by the top twenty thousand (20,000) private corporations to their local/resident supplier of goods and local/ resident supplier of services other than those covered by other rates of withholding tax*. - Income payments made by any of the top twenty

thousand (20,000) private corporations, as determined by the Commissioner, xxx. For this purpose, an agricultural product in their original state as used in these Regulations, shall only include corn, coconut, copra, palay, rice, cassava, coffee, fruit, vegetable, marine food product, poultry and livestock.

XXX XXX XXX

(S) *Income payments made to suppliers of agricultural products*. – Income payments made to agricultural suppliers such as, but not limited to, payments made by hotels, restaurants, resorts, caterers, food processors, canneries, supermarkets, livestock, poultry, fish and marine product dealers, hardwares, factories, furniture shops and all other establishments, in excess of the cumulative amount of Three Hundred Thousand Pesos (P300,000.00) within the same taxable year. - One percent (1%);

The term “agricultural suppliers” refers to suppliers/sellers of agricultural, forest and marine food and non-food products, livestock and poultry of a kind generally used as, or yielding or producing foods for human consumption, and breeding stock and genetic materials therefor. “Livestock” shall include cow, bull and calf, pig, sheep, goat and other animals similar thereto. “Poultry” shall include fowl, duck, goose, turkey and other animals similar thereto. “Marine product” shall include fish and crustacean such as, but not limited to, eel, trout, lobster, shrimp, prawn, oyster, mussel and clam, shell and other aquatic products.

Meat, fruit, fish, vegetable and other agricultural and marine food products, even if they have undergone the simple processes of preparation or preservation for the market, such as freezing,drying, salting, smoking or stripping, including those using advanced technological means of packaging, such as shrink wrapping in plastics, vacuum packing, tetra-pack and other similar packaging method, shall still be covered by this subsection.

An agricultural food product shall include, but shall not be limited to the following: corn, coconut, copra, palay, cassava, coffee, etc. Polished and/or husked rice, corn grits and ordinary salt shall be considered as agricultural food products.

XXX XXX XXX

(W) *Income payments made by the top five thousand (5,000) individual taxpayers to their local/resident suppliers of goods and local/resident suppliers of services other than those already covered by other rates of withholding tax*. - Income payments made by the top 5,000 individual taxpayers engaged in trade or business in the Philippines, as determined by the Commissioner xxx For this purpose, agricultural products in their original state as used in these Regulations, shall include only corn, coconut, copra, palay, rice, cassava, coffee, fruit, vegetable, marine food product, poultry and livestock.

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(Z) *Income payments to Real Estate Investment Trusts (REITs)*. – Income payments made to corporate taxpayers duly registered with the Large Taxpayers Regular Audit Division 3 (now Regular

LT Audit Division 3) of the Bureau of Internal Revenue, as REITs for purposes of availing of the incentive provisions of Republic Act No. 9856, otherwise known as “The Real Estate Investment Trust Act of 2009”, as implemented by RR No. 13- 2011. – One percent (1%);

(AA)*Income payments on locally produced raw sugar*. – Proprietors or operators of sugar mills/refineries on their mill share, and direct buyers of Quedans or Molasses Storage Certificates from the sugar planters on locally produced raw sugar and molasses shall withhold the creditable income tax and remit the same to the BIR based on the applicable base price of ONE THOUSAND PESOS (P1,000.00) per FIFTY (50) kilogram (kg.) bag and FOUR THOUSAND PESOS (P4,000.00) per metric ton, respectively, subject, however, to adjustment, when deemed necessary by the Commissioner, upon consultation with the Administrator of the Sugar Regulatory Administration (SRA). – One percent (1%).

For purposes of this subsection, the following terms shall have the following meaning:

i. *Buyers of Quedan or Molasses Storage Certificates* – refer to traders or industry users duly accredited by the SRA who bid and/or purchase the Quedans or Molasses Storage Certificates from the sugar planters.

ii. *Mill Share* – refers to payments to a sugar mill/refinery by the sugar planter for the milling of sugarcane. As such, it is equivalent to a sale of locally produced raw sugar.

iii. *Molasses Storage Certificate* – refers to the warehouse receipt issued by a sugar mill/refinery to the owner, as stated therein, attesting to the fact that the volume of molasses is stored at the mill’s facilities, with the commitment that it will be delivered to the holder of said document upon demand.

iv. *Sugar Mill/Refinery* – refers to a domestic company engaged in the business of milling sugarcane into raw sugar, or in the refining of raw sugar.

v. *Sugar Planter* – refers to the original owner of sugarcane brought to the mill for milling purposes.

vi. *Sugar Regulatory Administration (SRA)* – refers to an agency of the Philippine government under the Department of Agriculture, responsible for promoting the growth and development of the sugar industry, through greater participation of the private sector, and for improving the working conditions of the laborers, created by Executive Order No. 18, Series of 1986.

vii. *Quedan* – refers to a warehouse receipt issued by a sugar mill/ refinery to the owner as stated therein, attesting to the fact that the volume and class of sugar is kept at the said sugar mill/refinery, and with the commitment that it will be delivered to the holder of said document by the sugar mill’s/ refinery’s warehouseman upon demand. Quedan is issued in the name of the proprietor or operator of the sugar mill/refinery, for its mill

share, and to the sugar planter, as owner of the sugarcane, as certified by SRA representative at the sugar mill/refinery.

viii. *Trader* – refers to a domestic company or person given the authority and license by the SRA to engage in the business of trading sugar, molasses, or muscovado, as the case may be.

The Regional Director, through the recommendation of the Revenue District Officer, which has jurisdiction over the physical location of the sugar mills/refineries, shall issue the Authorization Allowing the Release of Locally Produced Raw Sugar/Molasses (Annexes "A" or "B", as applicable) to the proprietors or operators, for purposes of allowing the transfer/withdrawal of their mill share, or to the buyers of Quedans or Molasses Storage Certificates on the locally produced raw sugar, or molasses, for further processing into a refined sugar, consumption or other purposes: Provided, however, that, copies of proofs of payment of the creditable withholding tax due thereon (i.e., duly validated Monthly Remittance Return of Creditable Income Taxes Withheld (Expanded) [BIR Form No. 1601-E] and Bank Payment/Deposit Slip/ Revenue Official Receipt [BIR Form No. 2524]) shall have been submitted and attached to the written request for said authorization.

Provided, finally, That, notwithstanding the presentation of proof of exemption from the payment of income tax (e.g., BIR ruling, special law, etc.), the concerned proprietor, or operator of the sugar mill/ refinery, or any buyer of Quedan or Molasses Storage Certificate is stil required to withhold and remit the creditable withholding tax."

► These Regulations shall take effect on January 1, 2015 following publication in a newspaper of general circulation.

(Editor's Note: RR No. 11-2014 was published in the Manila Bulletin *on December 23, 2014.)*

Revenue Memorandum Circular No. 82-2014 dated November 20, 2014

RMC No. 82-2014 publishes the full text of Joint Circular No. 002-2014 of the DOF, DBM, BOC and BIR, which prescribes the mechanism for qualified VAT-registered persons to receive the cash equivalent of their outstanding VAT TCCs.

► *Definitions:*

1. VAT TCC – refers to any of the following TCCs issued in accordance with existing laws and regulations to the taxpayer named therein, acknowledging that the grantee-taxpayer named therein is entitled to a tax credit:

    ► Import VAT TCC – VAT TCC issued solely by the BOC pursuant to Section 112 of the Tax Code;
    ► VAT Drawback TCC – TCC issued jointly by the BOC and the One-Stop Shop Inter-Agency Tax Credit and Duty Drawback Center (DOF-OSS) pursuant to Section 106 (e) of the Tariff and Customs Code of the Philippines (TCCP);
    ► VAT TCC issued solely by the BIR pursuant to Section 112 of the Tax Code; and
    ► VAT TCC issued jointly by the BIR and the DOF-OSS pursuant to Section 122 of the Tax Code.

2. Monetization – refers to the mechanism of granting the cash equivalent of VAT TCCs under Section 3(A) of this Joint Circular.

3. Cash Conversion – refers to the mechanism of granting the cash equivalent of VAT TCCs under Section 3(B) of this Joint Circular.

4. Revalidation – refers to the one-time extension of the validity period of TCCs prior to their expiration at the end of the fifth (5th) year from the date of issue of the original TCC.

- *Coverage*

1. The following VAT TCCs are qualified for monetization:

   - VAT TCCs for which the BIR had issued the corresponding Notices of Payment Schedule (NPS) pursuant to Executive Order (EO) No. 68, series of 2012, and DOF-BIR-DBM joint Circular No. 2-2012; and
   - VAT Drawback TCCs approved for monetization by the BOC pursuant to EO No. 68, series of 2012, and DOF-BOC-DBM Joint Circular No. 3-2012.

2. The following VAT TCCs are qualified for cash conversion, notwithstanding the existing administrative regulations, guidelines or conditions prohibiting or restricting the cash conversion of VAT TCCs:

   - All other VAT TCCs outstanding as of 31 December 2012 which are not covered by the immediately preceding subsection; and
   - VAT TCCs issued after December 31, 2012.

- *Monetization of VAT TCCs with BIR-issued NPS*

1. Holders of NPS may present the same to the BIR for payment at any time, on or before the maturity dates indicated in the NPS.

2. Upon presentation of the NPS to the BIR by the NPS holder or his authorized representative, the BIR shall pay the amount indicated in accordance with existing budgeting, accounting and auditing law, rules and regulations. RMC No. 82-2014 publishes the full text of Joint Circular No. 002-2014 of the DOF, DBM, BOC and BIR, which prescribes the mechanism for qualified VAT- registered persons to receive the cash equivalent of their outstanding VAT TCCs.

3. Within 45 calendar days from the presentation of the NPS, the BIR shall directly pay the amount equivalent to the total face value of said NPS, net of any delinquent tax liability, to the account of the NPS holder, pursuant to the Modified Disbursement Payment System (MDPS) of the government.

   - For NPS presented on or before the 15th day of the month, the 45-day processing period shall commence on the first day of the immediately following month.
   - For NPS presented after the 15th of the month, the 45-day processing period shall commence on the 16th day of the immediately following month.

- *Monetization of Import VAT-TCCs and VAT Drawback TCCs*

1. The BOC shall, within 10 days from the date of effectivity of this Circular, send written notices advising holders of import VAT TCCs and VAT Drawback TCCs qualified for monetization that the corresponding cash equivalent thereof may be claimed from the BOC, subject to existing budgeting, accounting and auditing law, rules and regulations.

2. Qualified import VAT TCC holders are given one year from receipt of such notice to claim payment from the BOC.

3. Within 45 calendar days from the presentation of the notice, the BOC shall directly pay the amount equivalent to the outstanding balance of the TCC, net of any delinquent tax liability, to the account of the TCC holder, pursuant to MDPS of the government.

    - For notices presented on or before the 15th month, the 45-day processing period shall commence on the first day of the immediately following month.
    - For notices presented after the 15th of the month, the 45-day processing period shall commence on the 16th day of the immediately following month.

- *Cash Conversion of VAT TCCs*

1. Applications for cash conversion of Import VAT TCCs and Drawback VAT TCCs shall be filed directly with the BOC, while those for cash conversion of all other VAT TCCs shall be filed directly with the BIR.

2. An application shall be deemed complete if it is accompanied by the following documents:

    - Letter of Application;
    - Original TCC;
    - Proof of authority of representative: (a) Secretary's Certificate on the Board Resolution designating the TCC holder's authorized representative in the case of corporations, and (b) Special Power of Attorney in the case of partnerships and sole proprietorships, and;
    - For import VAT and VAT Drawback TCCs, a certification from the BOC Collection Service that the applicant has no tax and/or duty liabilities or a statement of the outstanding account, as the case may be.

3. The application shall be evaluated against the following criteria:

    - That the TCC was duly issued by the government;
    - That there is no tampering on the certificate;
    - That the requesting party is the rightful TCC owner;
    - That the TCC is not yet expired; and
    - That the TCC has remaining creditable/outstanding balance.

4. Within 45 calendar days from the filing of the application, the BIR or BOC, as the case may be, shall pay the amount equivalent to the outstanding balance of the TCC, net of any delinquent tax liability, to the account of the TCC holder, pursuant to MDPS of the government.

    - For applications filed on or before the 15th of the month, the 45-day processing period shall commence on the first day of the immediately following month.
    - For applications filed after the 15th month, the 45-day processing period shall commence on the 16th day of the immediately following month.

- *Rights of TCC Holders*

A holder of a covered VAT TCC who fails or does not intend to avail of the provisions of this Circular shall retain the right to:

- Credit his VAT TCCs against tax and/or duty liabilities in accordance with existing rules on TCC utilization;
- Apply, subject to conditions of law and pertinent rules and regulations, for VAT-TCC revalidation under Section 230(B) of the Tax Code.

- *Non-Issuance of VAT TCCs by the BIR and the BOC*

Upon the effectivity of EO No. 68-A, the BIR and the BOC shall no longer issue VAT TCCs, unless applied for by the VAT taxpayer pursuant to Section 112 (A) of the Tax Code or Section

106 (e) of the TCCP, in which c ase taxpayers who apply for, and are issued, VAT TCCs may apply for cash conversion.

Revenue Memorandum Circular No. 86-2014 dated December 5, 2014

RMC No. 86-2014 clarifies the valuation of contributions or gifts actually paid or made, in computing taxable income as part of substantiation requirements under RR No. 13-98.

- Section 8 of RR No. 13-98 requires donors claiming donations and contributions to an accredited non-stock, non-profit corporation/NGO as tax deductions to submit to the BIR a C ertificate/s of Donation, indicating the following: (a) actual receipt by the accredited non-stock, non-profit corporation/NGO of the donation or contribution and the date of receipt thereof; and (b) the amount of the charitable donation or contribution, if in cash, and if property, whether real or personal, the acquisition cost of the said property.

- The information required under RR No. 13-98 shall be declared in a Certificate of Donation (BIR Form No. 2322) in the format prescribed under this Circular.

- BIR Form No. 2322 consists of 2 parts: (a) a donee c ertification; and (b) a donor's statement of values:

    1. The donee certification, which is signed by an authorized representative of the donee organization, shall state the following:

        - Date of receipt of the subject matter of the donation, whether cash or property;
        - Description of the donated properties

    2. The donor's statement, which is signed by the donor or authorized representative, shall provide the description, acquisition cost and net book value of the donated properties, and shall be accompanied by the deed of sale/ bill of sale to prove the acquisition cost of the properties.

Revenue Memorandum Circular No. 89-2014 dated December 19, 2014

RMC No. 89-2014 clarifies the implementation of the increase in excise tax rates on locally manufactured cigarettes effective January 1, 2015 pursuant to RR No. 17-2012 implementing RA No. 10351, in relation to the new internal revenue stamps prescribed under RR No. 7-2014 as amended.

- All local manufacturers of cigarettes shall compute and pay the differential increase between the new excise tax rates and the current rates, according to the tax classification of their cigarette products, based on the number of internal revenue stamps, whether or not actually affixed to the packs of cigarettes, being held in their possession as of December 31, 2014.

- The total excise taxes shall be paid to the BIR not later than the last working day of December 2014.

- For purposes of validating the said tax payment, a physical inventory of all internal revenue stamps held in possession by all manufacturers of cigarettes as of December 31, 2014, whether or not actually affixed on cigarette packs, shall be conducted by BIR authorized representatives.

- The inventory shall be reconciled with the BIR Internal Revenue Stamp Integrated System (IRSIS) and in case of discrepancy, the deficiency excise taxes shall assessed and collected upon demand.

BOC Issuances

Customs Memorandum Order No. 28-2014 dated December 16, 2014

CMO No. 28-2014 prescribes the procedure for the cash refund of input VAT on importations attribute to zero-rated transactions under Section 112 of the Tax Code.

► *Coverage*

CMO No. 28-2014 covers all claims for refund of input VAT on importations attributable to zero-rated transactions under Section 112 of the Tax Code.

► *Operational Provisions*

1. Upon receipt of the docket from the BIR approving the claim of a particular importer for refund of the input VAT on his importation, the Tax Credit Secretariat (TCS) shall check that the following are included in the docket:

    ► Copy of the claimant's application for VAT refund;
    ► BIR endorsement to the BOC containing its determination of the validity of the claim for VAT refund on importation, with the corresponding Authority for the BOC to issue VAT credit/refund; and
    ► Original or certified true copies of the import entry and internal revenue declarations (IEIRDs), BOC Official Receipts or the Statement of Settlement of Duties and Taxes, Single Administrative Documents and List of Importations for the period of the claim.

2. If the above documents are found to be complete, the entire docket shall be endorsed to the Chief, Revenue Accounting Division (RAD) of the BOC for verification of payments of duties and taxes, using tax credits or if cash payments, the amounts must have been remitted to the Bureau of Treasury (BTr).

3. After receipt of the docket from the Chief, RAD and his certification attesting collection and remittance to the BTr of the payment/s made, the TCS shall in turn endorse the docket to the Chief Accountant, Accounting Division, Financial Management Office (FMO) for validation and computation of the amount to be refunded based on the certification of payment issued by RAD, and issue and Evaluation Report thereon.

4. Upon receipt of the docket from the FMO with the corresponding Evaluation Report, the TCS shall determine whether the claimant will avail of a cash refund or for the issuance of TCC.

5. The Secretariat shall then prepare the corresponding endorsement for signature of the Commissioner, or his duly authorized Tax Credit Approving Authority, authorizing payment of the cash refund or issuance of a Tax Credit Certificate based on the amount computed or recommended by the FMO. The signed resolution/endorsement authorizing payment shall be forwarded to the Accounting Division, FMO for preparation of the cash refund or issuance of TCC.

► *Manner of Payment of Cash Refund*

1. The release of cash payment for refund of VAT on importation shall be subject to the availability of funds appropriated for the purpose.

2. The procedure in budget execution shall be subject to existing budgeting laws, rules and regulations, in consultation with the DBM.

► *Clearance of No Outstanding Liability*

1. Claimants shall be required to secure a Clearance from the Collection Service attesting that the importer-claimant has no outstanding liability with the BOC, which shall be submitted to the TCS before preparation of the Endorsement authorizing payment.

2. In cases where a particular claimant has determined liabilities as borne by the records of the Collection Service, he shall be required to settle first his liabilities before his claim for VAT refund will be processed for payment.

► *Treatment of Pending Applications*

Applicants whose claims are pending processing with the BOC, or those whose TCCs have yet to be issued, are given the option to apply for a cash refund upon submission of a formal letter to the TCS manifesting their preference for payment of cash refund in lieu of TCCs.

► CMO No. 28-2014 took effect immediately upon signing thereof on December 16, 2014.

Customs Administrative Order No. 8-2014 (no date supplied)

CAO No. 8-2014 prescribes the guidelines on the imposition of the Customs Documentary Stamp (CDS) and Import Processing Fee (IPF) for Informal Entries.

► The CDS and IPF rates for informal entries in all ports of the Philippines shall beas follows:

1. Revised Amount of CDS – P15 for each importation filed through the informal entry
2. IPF – No amount shall be collected as IPF on any importation filed through the informal entry. The BOC shall cease to collect IPF on any importation filed through the informal entry.

► CAO No. 8-2014 shall take effect immediately upon publication in a newspaper of general circulation or the Official Gazette and three copies are deposited in the UP Law Center.

(Editor's Note: CAO No. 8-2014 was published in The Manila Times *on December 10, 2014.)*

DOF Issuance

Department Order No. 107-2014, dated November 28, 2014

DOF DO No. 107-2014 prescribes updated rules on accreditation of PEZA locators with the BOC.

► All locators of PEZA Special Economic Zones throughout the Philippines, duly registered with PEZA, are exempted from the requirements of DOF DO No. 12-2014 as amended by DO No. 18-2014, and shall be eligible for accreditation as importers with the BOC Account Management Office (BOC-AMO).

► The BOC may still require the submission of documents and information about PEZA locators prior to granting accreditation. Whenever possible, the BOC shall obtain the documents and information it needs about PEZA locators from the documents and information already in the possession of PEZA.

► PEZA locators that will import goods into the Philippines will have to comply with the documentary requirements provided in the relevant rules of procedure of customs. Failure to do so will subject them to sanctions and penalties as provided by the TCCP.

► The Commissioner of Customs shall issue rules and regulations pursuant to this Order within 15 days from issuance.

► All orders, circulars, memoranda, issuances contrary to or inconsistent therewith are hereby revoked and / or modified, and all concerned shall be guided accordingly.

► DOF DO No. 107-2014 took effect immediately.

Court Decisions

Waterfront Philippines, Inc. vs. CIR

CTA *(En Banc)* Case No. 1070 promulgated December 4, 2014

Interest income from loans and advances to affiliates is considered as revenue realized from services rendered in the normal course of trade or business and is subject to 12% VAT.

Facts:

Respondent Commissioner of Internal Revenue (CIR) assessed Petitioner Waterfront Philippines, Inc. (Waterfront) for alleged deficiency taxes for taxable year 2006, including VAT on interest income derived from loans granted to affiliates.

The CIR claims that in the ordinary course of business, Waterfront extends and obtains cash advances and loans to and from related parties to meet working capital requirements and to finance the construction and operation of its hotel projects, in furtherance of the primary purpose stated in the Articles of Incorporation. The CIR alleges that said interest income is subject to VAT. Waterfront protested the assessment.

Upon denial of its protest by the CIR, Waterfront filed a Petition for Review with the Court of Tax Appeals (CTA). The CTA First Division initially ruled that the interest income from loans or advances granted to affiliates by Waterfront, which is not engaged in the business of lending money, is not subject to VAT.

The CIR filed a Motion for Reconsideration and argued that Waterfront was assessed for deficiency VAT not as a lending investor but for interest income realized from loans and advances granted to related parties in the ordinary course of trade or business. The CTA First Division issued an Amended Decision ordering Waterfront to pay the assessed deficiency VAT. Upon denial of its Motion for Reconsideration of the Amended Decision, Waterfront filed a Petition for Review with the CTA *En Banc*.

Issue:

Is the interest income derived by Waterfront from loans and advances granted to affiliates subject to VAT?

Ruling:

Yes. The interest income from loans and advances extended by Waterfront to its affiliates is considered revenue from services rendered in the ordinary course of trade or business and is subject to VAT.

Section 105 of the Tax Code defines “in the course of trade or business” as the regular conduct or pursuit by any person of a commercial or an economic activity, including transactions incidental thereto. Section 108 of the Tax Code also provides that VAT is due on the “sale or exchange of services” or the performance of all kinds of services in the Philippines for others for a fee or consideration regardless of whether the performance of such services calls for the exercise or use of physical or mental faculties.

The CTA cited *Diaz, et al. vs. Secretary of Finance, et al.* promulgated on July 19, 2011, where the Supreme Court held that VAT is imposed on all kinds of services in the Philippines for a fee. The enumeration of services subject to VAT in Section 108 of the Tax Code is not exclusive. The listing of specific services illustrates how broad the VAT coverage is. Every activity that can be imagined as a form of service rendered for a fee should be deemed included unless a specific

provision of law excludes it. Waterfront failed to point to a provision of law that specifically excludes extending cash advances with interest to affiliates to the definition of services subject to VAT.

Waterfront extended cash advances to its affiliates, which is clearly a performance of service for a fee (with interest as the fee or consideration) that is covered by the VAT provisions of the Tax Code. While the act of extending cash advances with interest to affiliates may be an isolated transaction, the same is incidental to the course of trade or business as said activity is within the ambit of the 'catch-all' purpose stated in Waterfront's Amended Articles of Incorporation, wherein the corporation is authorized "to do any and all things necessary, suitable, convenient, proper or incidental to the accomplishment of the above purposes."

The CTA likewise cited the Supreme Court's decision in *CIR vs. COMASERCO* promulgated on March 30, 2000 where it was ruled that as long as the entity provides a service for a fee, remuneration or consideration, then the service is subject to VAT. Applying the *COMASERCO* and *Diaz* cases, the CTA *En Banc* held that extending cash advances with interest to related parties is a form of service for a fee, for which VAT may be imposed.

Visayas Geothermal Power Company vs. CIR

CTA (First Division) Case 8425 promulgated November 17, 2014

Service fees payable by a Philippine company to a non-resident foreign corporation are exempt from the FWT if it can be established that (a) the services are performed by a foreign corporation not engaged in trade or business in the Philippines, and (b) the said income is derived from sources outside the Philippines.

Moreover, to be exempt from withholding VAT, it must be proved that the (a) payee is a non-resident foreign corporation, and (b) the services were rendered outside the Philippines.

Facts:

Respondent CIR assessed Visayas Geothermal Power Company (VGPC) for deficiency FWT and final withholding VAT for taxable year 2002 on service fees paid to MidAmerican Energy Holdings Company (MidAmerican), a US corporation.

The CIR alleged that VGPC failed to declare and pay in its monthly remittance returns the FWT and withholding VAT due on the fees paid to MidAmerican covering corporate management, financial planning support, and technical and administrative support services for the operation of a power plant in the Philippines, as provided under a Service Agreement.

VGPC protested the assessment and argued, among others, that MidAmerican Energy's services were performed outside the Philippines. VGPC also claimed that the CIR's right to assess deficiency taxes for taxable year 2002 has prescribed.

Issues:

1. Are the service fees paid by VGPC to MidAmerican Energy subject to FWT?
2. Are the service fees subject to withholding VAT?
3. Has the right of the CIR to assess VGPC prescribed?

Ruling:

1. Yes. Section 28 (B) (1) of the Tax Code prescribes that a non-resident foreign corporation is liable for income tax on income derived from all sources within the Philippines. VGPC failed to prove that the CIR's assessment is incorrect. Tax assessments by tax examiners are presumed correct and made in good faith. All presumptions are in favor of the correctness of a tax assessment unless proven otherwise. In order for a non-resident foreign corporation to not be subjected to FWT, it must prove that it is (a) a foreign corporation not engaged in business in the Philippines; and (b) its source of income is outside the Philippines. VGPC failed to establish that

the services were rendered outside the Philippines. The Service Agreement merely stipulates the kinds of services that will be performed by MidAmerican but not the manner and the place where the said services will be performed.

2. Yes. Section 108 (A) of the Tax Code prescribes a 12% VAT on the 'sale or exchange of services' performed in the Philippines.

To be exempt from withholding VAT, VGPC must prove that (a) MidAmerican is a non-resident foreign corporation, and (b) the services were rendered outside the Philippines. Although VGPC proved that MidAmerican Energy is a non-resident foreign corporation, it failed to prove that the services were performed outside the Philippines.

3. No. The right of the CIR to assess VGPC has not yet prescribed. While taxes should be assessed within 3 years after the last day prescribed by law for the filing of the return, the prescription is extended to 10 years in the case of a false or fraudulent return.

Since VGPC failed to prove that MidAmerican Energy's income is derived from sources outside the Philippines and that it rendered services outside the Philippines, the FWT and VAT returns are considered false, justifying the application of the 10-year prescriptive period.