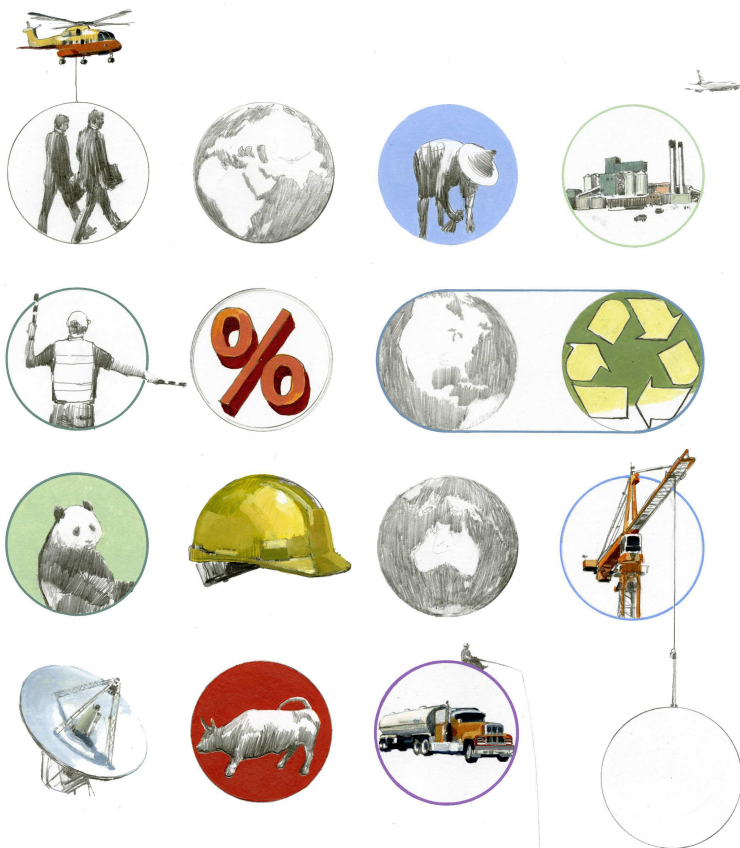


October 2010

Tax brief



Contents

02 SEC Circular

- Extended deadline for anti-money laundering manual

02 Court Decisions

- EWT on telephone directory listing
- Deductibility of rental paid to affiliates
- Non-submission of supporting documents in the administrative level not fatal to judicial claim for refund
- Period for filing judicial claims for refund
- Application of most favored nation clause under RP-US tax treaty

04 BIR Issuances

- Removal of VAT exemption on electricity and water consumption of senior citizens
- Abatement program for voluntary tax payments
- Issuance of certificate of tax exemption of cooperatives

07 BIR Rulings

- FCDU exemption covers GRT
- Tax status of employees assigned abroad

08 Highlight on P&A services

- Corporate organization and registration

SEC Circular

Extended deadline for anti-money laundering manual

The Securities and Exchange Commission (SEC) has extended the deadline for submission of the revised anti-money laundering manual from September 8, 2010 to December 8, 2010 to allow covered institutions to prepare and comply with the revised guidelines in the preparation of anti-money laundering operating manual.

The submission of the revised anti-money laundering manual by the covered institutions was required by the SEC under Memorandum Circular No. 2, series of 2010, last May 20, 2010 in conformity with the provisions of Republic Act No. (RA) 9194, as amended by RA 9160, otherwise known as the Anti-Money Laundering Act of 2001. "Covered institutions" refers to persons regulated by the SEC, such as securities dealers and brokers, investment houses, investment companies, and financial and lending companies.

Non-submission of the revised anti-money laundering manual will subject the covered institution to a penalty of P500 per day of delay until the manual is submitted to the SEC.

(SEC Memorandum Circular No. 8, Series of 2010, September 23, 2010)



Court Decisions

EWT on telephone directory listing

Income payments made by a holding company to a telecommunication company for advertising and publishing its telephone number in the telephone directory are not considered income payment made to an advertising company subject to 1% (now 2%) expanded withholding tax (EWT). The publication of the telephone directory by the telecommunication company does not make it an advertising company.

However, the Court of Tax Appeals (CTA) held that while it is not considered an advertising company, the income payment made by the holding company to the telecommunication company should be subject to 2% EWT imposed on income payments to "other contractors," particularly printers, bookbinders, lithographers and publishers under Section 2.57.2(E)(4)(f) of RR 2-98.

(Covanta Energy Philippine Holdings, Inc. v. Commissioner of Internal Revenue, CTA Case No. 7103, September 15, 2010)



Court Decisions

Deductibility of rental paid to affiliates

In a decision of the CTA in division, the court upheld the disallowance of the BIR of the rent expense claimed by a domestic car manufacturing company on the ground that it is a shareholder of the corporation that owns the rented property. The CTA in division cited Section 29(a)(1)(A) of the 1977 Tax Code [now Section 34(A)(1)(a)(iii), Tax Code], which provides that for rent expense to be deductible for income tax purposes, the taxpayer should have no equity to the property being rented.

Acting on the appeal made by the taxpayer, the CTA en banc held that the company cannot be deemed to have title to or equity in the properties owned by its affiliates as contemplated under Section 29(a)(1)(A) of the 1977 Tax Code on the ground that it has equity in the corporation that owns the leased property. The CTA en banc clarified that said Section refers to the equity in the property itself and not to equity in the corporations that own the property subject of lease.

As explained by the CTA en banc, a corporation has a personality distinct and separate from its individual stockholders or members, and is not affected by the personal rights, obligations and transactions of the latter. As lessee, the company cannot be deemed to have equity in the properties owned by or registered in the name of the affiliates without violating the doctrine of separate and distinct juridical personality of the corporation. Extending the condition stated under Section 29(a)(1)(A) of the 1977 Tax Code to the property owned by a corporation, which has a separate and distinct juridical personality, will unduly impose upon the company a burden that is not in the law.

(Mitsubishi Motors Philippines Corporation v. Commissioner of Internal Revenue, CTA EB No. 526 re CTA Case No. 6385, September 7, 2010)

Non-submission of supporting documents in the administrative level not fatal to judicial claim for refund

Although the submission of complete documents is necessary to support a claim for refund, failure of the taxpayer to submit the complete documents at the administrative level does not bar the CTA from receiving, evaluating and appreciating evidence in support of the taxpayer's claim for refund or issuance of tax credit certificate.

In judicial claims for refund, the question of whether or not the evidence submitted by a party is sufficient to warrant the granting of a claim lies within the sound discretion and judgment of the court. According to the CTA, judicial claims are decided based on what has been presented and formally offered, and not on mere allegation of non-submission of complete documents before the BIR. Conversely, unless the documentary evidence submitted by the taxpayer to the BIR is formally offered before the CTA, they have no evidentiary value.

(Commissioner of Internal Revenue v. Toledo Power Company, CTA EB No. 589 re CTA Case No. 7471, September 15, 2010)

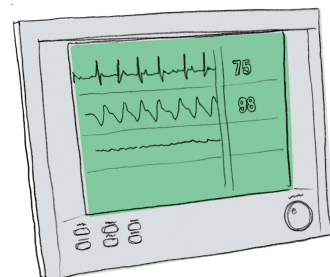
Period for filing judicial claims for refund

Under Section 112(D) of the Tax Code, the Commissioner of Internal Revenue (CIR) is given 120 days from the date of submission of complete documents to decide whether to grant a refund/issue tax credit certificate, or to deny the claim. If the CIR grants or denies the claim, or in case he fails to act within the 120-day period, the taxpayer may appeal the decision or the unacted claim to the CTA within 30 days from receipt of the decision, or after the expiration of the 120-day period.

In the instant case, the taxpayer filed its administrative claim for refund/issuance of tax credit certificate of its unutilized input VAT on January 4, 2007, which falls within the two-year prescriptive period from the close of the taxable quarter when the sales were made. Pursuant to Section 112(D) of the Tax Code, the CIR has 120 days or until May 4, 2007 to decide on the taxpayer's administrative claim. Since the CIR failed to act on the claim for refund, the taxpayer had 30 days from May 5, 2007, or up to June 3, 2007, to appeal the inaction of the CIR. The taxpayer filed its judicial claim on March 30, 2007, or 35 days before the lapse of the 120-day period to decide and commencement of the 30-day period to appeal to the CTA.

The claim was deemed prematurely filed by the CTA. According to the CTA, the taxpayer should have first exhausted the administrative process afforded to him before resorting to judicial remedy. Hence, due to failure to exhaust administrative remedies, the taxpayer's claim for refund/issuance of tax credit certificate of its unutilized input VAT was denied.

(Mindanao II Geothermal Partnership v. Commissioner of Internal Revenue, CTA Case No. 7595, September 14, 2010)



Court Decisions

Application of most favored nation clause under RP-US tax treaty

The similarity in the circumstances of payment of taxes is a condition for the enjoyment of the most favored nation treatment under prevailing tax treaties. Thus, before applying the 10% preferential tax rate provided for in the Republic of the Philippines (RP) - Czech Tax Treaty on royalties paid by a domestic company to a US company pursuant to the “most favored nation” clause under RP-US Tax Treaty, it is important to establish that the taxes imposed upon royalties under RP-US Tax Treaty and RP-Czech Tax Treaty are paid under similar circumstances.



Based on a comparison made of the provisions of the RP-US Tax Treaty and RP-Czech Tax Treaty, the CTA held that while both tax treaties provide the credit method as a means of eliminating international judicial double taxation, it is not certain whether the limitation on the amount of credit under the RP-US Tax Treaty is similar to that stated under RP-Czech Tax Treaty. According to the CTA, reference still has to be made to the “United States law” to determine the limitation referred to in Article 23(1) of the RP-US Tax Treaty to determine the limitation. This is no longer necessary in the case of the RP-Czech Tax Treaty because it specifically provides that the deduction shall not exceed the part of the Czech tax that is appropriate to the income earned.

The CTA ignored the BIR ruling secured by the taxpayer expressly allowing the taxpayer to apply the 10% preferential tax rate on royalties since the BIR merely cited the provisions of the RP-US Tax Treaty and RP-Czech Tax Treaty and immediately jumped to conclusion without explaining that the mechanism employed by the United States is the same as that employed by the Czech Republic. Hence, in the absence of evidence showing that the taxes imposed upon royalties in the RP-US Tax Treaty and RP-Czech Tax Treaty are paid under similar circumstances, the taxpayer cannot claim the 10% preferential tax rate under RP-Czech Tax Treaty. As a consequence, the CTA denied its claim for refund on the difference between the 15% tax rate the taxpayer paid on its royalty payments, and 10% preferential tax rate under the RP-Czech Tax Treaty.

(Cargill Philippines, Inc. v. Commissioner of Internal Revenue, CTA Case No. 7656, September 6, 2010)

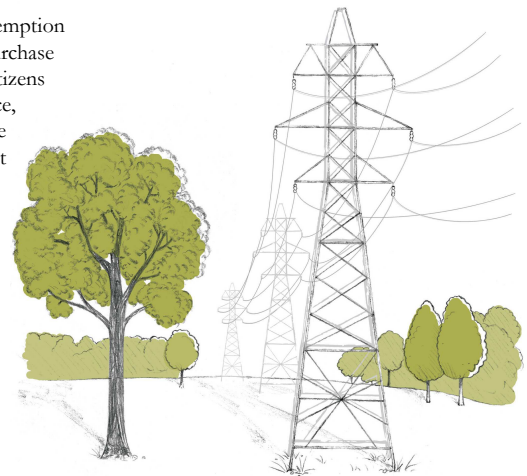
BIR Issuances

Removal of VAT exemption on electricity and water consumption of senior citizens

The BIR has removed the VAT exemption of electric and water consumption of senior citizens. These items were on the list of goods and services that were previously exempted from VAT under RR 07-2010, or the implementing regulations of RA 9994, or the Expanded Senior Citizens Act of 2010.

The BIR clarified that the VAT exemption under RA 9994 is limited to the purchase of goods and services of senior citizens entitled to the 20% discount. Hence, water and electricity bills, which are granted only a 5% discount, cannot be entitled to the VAT exemption.

(Revenue Regulations No. 08-2010, September 3, 2010)



BIR Issuances

Abatement program for voluntary tax payments

The BIR launched an abatement program, which gives taxpayers who will voluntarily file and pay their taxes and/or amend their tax returns to pay their correct tax liabilities the opportunity to settle their tax deficiencies without paying any surcharge and/or compromise penalties. The abatement program covers all tax types like income tax, VAT, estate tax, and creditable withholding tax.

The abatement program is available to all taxpayers who have not been issued a Letter of Authority (LA) or its equivalent for the tax period or for the return applied for the abatement program. As another condition to qualify for the program, the return or tax type should also not be the subject of any pending or final and executory court decision for criminal case for tax evasion and other criminal offenses under the Tax Code. In case an amended return is filed, the amendment should result in additional tax payment (increase in revenues or decrease in deductions or increase in both but resulting to a higher tax due) for the taxpayer.

Those who are interested in availing of the program must execute a declaration of availment of abatement and submit it to the BIR office where he is registered, with the following attachments, all in three copies:

- a. For original tax returns - Photocopy of the return filed and attachments and proof of payment of taxes
- b. For amended returns - Photocopy of the original and amended return, with attachments, and proof of payment for both

Filing and payment, including for returns relating to importations, may be done with an Authorized Agent Bank (AAB) or Revenue Collection Officer (RCO) within the taxpayer's RDO or through the eFPS in case of eFPS taxpayers. The declaration of availment of the abatement program must be filed on or before October 29, 2010.

An initial evaluation on the completeness of the application shall be done within two days from receipt, and approval/disapproval shall be issued within 30 days. Otherwise, the abatement shall be deemed approved.

(Revenue Regulations No. 09-2010, September 13, 2010)

Issuance of certificate of tax exemption of cooperatives

The BIR has issued the following guidelines in the processing and confirmation of the tax incentives granted to cooperatives under RA 9520.

A. Guidelines and procedures

In applying for certificate of exemption, the cooperative should observe the following guidelines and procedures:

1. All cooperatives previously registered with and confirmed by the Cooperative Development Authority (CDA) under RA 6938 and RA 6939 are deemed registered under RA 9520 (new Cooperative Code), and a new certificate of registration will be issued by the CDA.
2. All cooperatives must first secure their new certificate of exemption from the CDA before they can apply for Certificate of Tax Exemption from the BIR. The application should be filed and acted upon by the Revenue District

Office and Revenue Region having jurisdiction over the principal place of business of the cooperative.

3. All cooperatives applying for tax exemption shall be required to update their BIR registration with the RDO having jurisdiction over their principal place of business. The application for Registration Update of the cooperative may be processed simultaneously with its application for tax exemption.
4. The updated Certificate of Registration shall be issued and released by the BIR to the cooperative together with the Certificate of Tax Exemption within ten working days from the submission of complete documents.
5. The Certificate of Tax Exemption shall be valid for a period of five years from the date of issue or date of effectivity, unless it is revoked or cancelled. The original Certificate of Tax Exemption may be renewed by filing BIR Form 1945 and submitting all documentary requirements at least two months before the expiration of the certificate of exemption. The renewal certificate shall be valid for another five years, unless it is revoked for a cause.



BIR Issuances

B. Documentary requirements

The following documents should be filed with the BIR by cooperatives that are applying for certificate of tax exemption.

1. Original issuance of Certificate of Tax Exemption – Cooperatives that are applying for the first time for Certificate of Tax Exemption are required to submit a duly accomplished Application of Tax Exemption for Cooperatives (BIR Form 1945), together with the certified true copies of the following:
 - a. Articles of cooperation and bylaws, as certified by CDA
 - b. New certificate of registration issued by the CDA under RA 9520
 - c. Current certificate of good standing issued by the CDA effective on date of application
 - d. BIR certificate of registration

In addition, the cooperative should submit an original copy of certification under oath of the list of cooperative members with their respective Taxpayer Identification Number (TIN) and their capital contributions prepared by an authorized official of the cooperative. Those without TIN may temporarily use their National Statistics Office (NSO) number or other government issued ID number or Community Tax Certificate number. However, the cooperative must require all its members to secure a TIN for the updated list of members to be submitted together with the regular filing of the cooperative's annual income tax return.

2. Renewal of Certificate of Tax Exemption – To be attached to the duly accomplished BIR Form 1945 (Certificate of Tax Exemption for Cooperatives) are the certified true copies of the following documents:
 - a. Certificate of registration issued by the CDA under RA 9520
 - b. Latest articles of cooperation and bylaws of the cooperative
 - c. Current certificate of good standing from CDA, effective on the date of application
 - d. Latest financial statements of the immediately preceding year duly audited by a BIR accredited independent certified public accountant

All applications for tax exemption filed by cooperatives with the BIR Law Division prior to the issuance of the Revenue Memorandum Order (RMO) 76-2010 shall be transmitted to the concerned RDO for processing. Likewise, they shall also be required to update their BIR registration.

C. Reportorial requirements

The following documents and information are required to be submitted yearly to the BIR together with the filing of the cooperative's Annual Information Return (BIR Form 19702) due on or before the 15th day of the fourth month following the close of the calendar year:

1. Certified true copy of the current and effective certificate of good standing from CDA
2. Certified true copy of certification under oath by the chairperson/ general manager stating, among others, the type of cooperative, amount of accumulated reserves, and amount of net surplus for the year
3. Original copy of the yearly summary of records of transactions
4. Original copy of certification under oath by the chairperson/ general manager of the list of members, their respective TINs, and the share capital contribution of each member as of the year end concerned

(Revenue Memorandum Order No. 76-2010, September 28, 2010)



BIR Rulings

FCDU exemption covers GRT

The BIR has now recognized that the exemption of foreign currency deposit units (FCDUs) of banks from all taxes, as restored via RA 9294, covers the gross receipts tax (GRT).

Earlier, in BIR Ruling No. DA(FIT-002) 054-2010, the BIR held that FCDUs shall be subject to the 5% GRT on the interest income to be derived by FCDUs from the multi-currency retail treasury bonds (rTB) for overseas Filipino workers issued by the Bureau of Treasury.

After a careful re-study of the ruling, the BIR clarified that the interest income of FCDUs from the rTB are not subject to GRT. The BIR explained that the restoration of the tax exemption of FCDUs by RA 9294, which adopted the same provision including the phrase “exempt from all taxes” as originally provided under the 1977 Tax Code, presupposes the re-enactment of administrative interpretation of the legislative provisions that were restored granting tax exemption to FCDUs.

In RR 10-76, which implemented the old law, the BIR interpreted the phrase “exempt from all taxes” to mean that FCDUs are exempt from, among others, the GRT. The provision under the current National Internal Revenue Code (NIRC) uses the same phrase — “exempt from all taxes” — as previously provided under the 1977 Tax Code. Thus, under the principle of legislative approval of administrative interpretation by reenactment, RR 10-76, which was the implementing regulation of the old law exempting FCDUs from gross receipts tax, among others, is therefore deemed re-enforced.

(BIR Ruling No. 051-2010, September 7, 2010)

Tax status of employees assigned abroad

Filipino employees of a foreign company who are assigned abroad for less than 183 days are still considered resident citizens of the Philippines subject to the Philippine income tax on income derived from services performed within and outside the Philippines.

Under Section 22(E) of the Tax Code, in order for the employees to be considered non-resident citizens, the employees should be assigned abroad for more than 183 days during a taxable year. Hence, if the assignment period is less than 183 days, they do not fall within the definition of non-resident citizens. As such, their compensation income, even if paid by a foreign employer through an agent in the Philippines, is subject to the Philippine income tax imposed under Section 24(A) of the Tax Code.

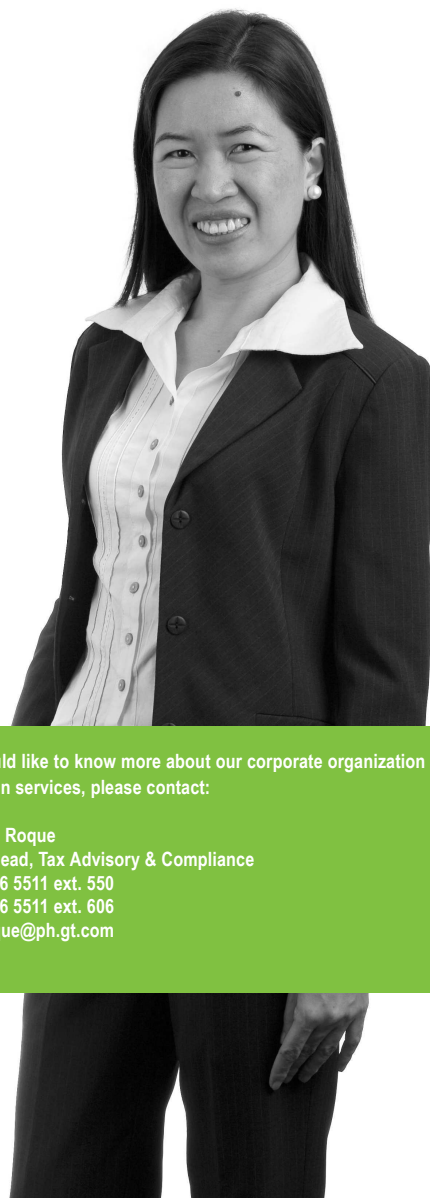
(BIR Ruling No. 052-2010, September 7, 2010)



Highlight on P&A services

Corporate organization and registration

We render advisory services and assistance on the implementation of, and in obtaining required government approvals for, a client's plan to undergo various types of corporate restructuring arrangements such as increase or decrease of capital stock, conversion of debt to equity, undergoing equity restructuring or quasi-reorganization, dividend declaration or profit repatriation, or any other amendments to a company's Articles of Incorporation and/or By-Laws. We also assist in analyzing, implementing and securing required government approvals for mergers, spin-offs of business units, and tax-deferred exchanges/transfers of properties for shares.



Tax Brief is a regular publication of Punongbayan & Araullo (P&A) that aims to keep its clientele, as well as the general public, informed of various developments in taxation and other related matters. This publication is not intended to be a substitute for competent professional advice. Even though careful effort has been exercised to ensure the accuracy of the contents of this publication, it should not be used as the basis for formulating business decisions. Government pronouncements, laws, especially on taxation, and official interpretations are all subject to change. Matters relating to taxation, law and business regulation require professional counsel.

We welcome your suggestions and feedback so that the Tax Brief may be made even more useful to you. Please get in touch with us if you have any comments and if it would help you to have the full text of the materials in the Tax Brief.

Lina Figueroa
Principal, Tax Advisory & Compliance Division
T +632 886-5511 ext. 507
F +632 886-5506 ext 606
E Lina.Figueroa@ph.gt.com

P&A is a member firm within Grant Thornton International Ltd. Grant Thornton International is one of the world's leading organizations of independently owned and managed accounting and consulting firms.

If you would like to know more about our corporate organization and registration services, please contact:

Eleanor L. Roque
Division Head, Tax Advisory & Compliance
T + 632 886 5511 ext. 550
F + 632 886 5511 ext. 606
E Lea.Roque@ph.gt.com