

Tax Bulletin

June 2017



Highlights

BIR Rulings

- ▶ The conveyance of property without monetary consideration by one government agency to another is exempt from Capital Gains Tax (CGT), regular corporate income tax and Documentary Stamp Tax (DST). **(Page 3)**
- ▶ Government educational institutions are exempt from tax on income used actually, directly and exclusively for educational purposes. They are also exempt from VAT on educational services. **(Page 4)**
- ▶ Rural banks formed through consolidation may enjoy the five-year tax exemption granted under RA No. 7353 or the Rural Banks Act of 1992 in case any or both of the constituent banks did not avail of the exemption, or for the remaining period in case the tax exemption was availed. **(Page 4)**

BIR Issuances

- ▶ Revenue Memorandum Circular (RMC) No. 42-2017 circularizes the revised BIR Form No. 2305, or the Certificate of Update of Exemption of Employer and Employee's Information. **(Page 5)**
- ▶ RMC No. 43-2017 announces the availability of new versions of the Update of Exemption of Employees (UEE) Data Entry Module that is used in filing BIR Form No. 2305. **(Page 5)**
- ▶ RMC No. 45-2017 publishes the full text of Executive Order (EO) No. 19 dated 27 April 2017, titled "Reduction and Condonation of Real Property Taxes and Interests/ Penalties Assessed on the Power Generation Facilities of Independent Power Producers (IPPs) under Build-Operate Transfer Contracts with Government-Owned or Controlled Corporations (GOCCs)". **(Page 6)**

BSP Issuances

- ▶ Circular No. 961 provides for Amendments to the Manual of Regulations for Banks and Non-Bank Financial Institutions as of 31 December 2016. **(Page 7)**
- ▶ Circular No. 962 provides for the Guidelines on the Method of Determining Compliance with the Required Basic Security Deposit During the Transition Period of Spun-off Trust Departments to Trust Corporations. **(Page 7)**

SEC Issuance

- ▶ An online English tutorial and diving school that offers its courses for a fee, and thereafter, issues a Diploma or Certificate for Program Completion is considered an educational institution subject to the nationality restrictions under the Constitution. **(Page 8)**

BOC Issuance

- ▶ CMO No. 13-2017 provides for the Standard Operating Procedure in the Usage and Handling of Weapons of Mass Destruction - Proliferation Prevention Program Provided Equipment under the National Coast Watch System and Conduct of Operation in the Detection, Interdiction and Control of Radioactive Materials. **(Page 9)**

PEZA Update

- ▶ PEZA Memorandum Order No. 2017-21 circularizes the roll-out of the PEZA e-Payment System, an application which allows locators to pay PEZA fees online. (Page 10)

BOI Updates

- ▶ BOI Memorandum Circular No. 2017-004 provides the general policies and specific guidelines for the registration of projects and availment of incentives under the 2017 Investment Priorities Plan (IPP). (Page 11)
- ▶ DTI-BOI Administrative Order No. 1 provides the implementing guidelines of EO No. 22, which extends for another year the duty-free incentive for importations of capital equipment and machinery, spare parts, and accessories of BOI-registered entities. (Page 27)

BLFG Opinions

- ▶ Gross receipts realized by a specialty contractor from its overseas construction projects are not subject to local business tax. (Page 29)
- ▶ Local Economic Enterprises are subject to income tax and VAT. (Page 30)

Court Decisions

- ▶ Where a Rehabilitation Court issues an Order calling for the suspension of the enforcement of claims against a distressed company, the BIR's act of sending a notice of informal conference and Formal Letter of Demand to the distressed company are considered acts of defiance of the Order.

The remedy of the BIR is to submit its claim to the Rehabilitation Court for proper consideration so that it may participate in the proceedings. (Page 31)

- ▶ The BIR has a period of five years following the assessment within which to collect the tax from a taxpayer. A request for a reduction, waiver, or compromise of penalties does not suspend the prescriptive period to collect the tax. (Page 33)

BIR Rulings

BIR Ruling No. 229-2017 dated 15 May 2017

The conveyance of property without monetary consideration by one government agency to another is exempt from CGT, regular corporate income tax and DST.

Facts:

The Department of Agriculture (DA), through its Secretary, executed a Deed of Assignment of a parcel of land in favor of the Bureau of Fisheries and Aquatic Resources ("BFAR") without any monetary consideration. By virtue of the Deed, BFAR applied for the issuance of a land title in its own name.

Issues:

1. Is the assignment subject to CGT or regular corporate income tax?
2. Is the Deed of Assignment subject to DST?

Ruling:

1. No. While the conveyance of property by the DA in favor of the BFAR was pursuant to a Deed of Assignment, the assignment was made without monetary consideration. Hence, it is not subject to CGT. Neither is it subject to the regular corporate income tax since the DA and the BFAR, which are both government agencies exercising purely governmental functions when the Deed was executed, are exempt from such regular corporate income tax.
2. Yes. The transaction is exempt from DST on conveyance of real properties for the same reason that the DA and the BFAR are both government agencies exercising purely governmental functions when the Deed was executed.

BIR Ruling No. 259-2017 dated 29 May 2017

Government educational institutions are exempt from tax on income used actually, directly and exclusively for educational purposes. They are also exempt from VAT on educational services.

Facts:

UP Los Baños, a Government educational institution, requested for a confirmation of its tax exemption under Section 30 (I) of the Tax Code.

Issues:

1. Is UP Los Baños exempt from income tax?
2. Is it entitled to other tax exemptions for educational services rendered?

Ruling:

1. Yes. Pursuant to Section 30 (I) of the Tax Code, in relation to Article XIV of the 1987 Philippine Constitution, Government educational institutions are exempt from tax on income used actually, directly and exclusively for educational purposes.
2. Yes. Section 109 (H) of the Tax Code provides that educational services rendered by a Government educational institution shall be exempt from 12% VAT. However, the exemption does not extend to purchases and importations of goods or properties, and purchases of services.

BIR Ruling No. 272-2017 dated 7 June 2017

Rural banks formed through consolidation may enjoy the five-year tax exemption granted under RA No. 7353 or the Rural Banks Act of 1992 in case any or both of the constituent banks did not avail of the exemption, or for the remaining period in case the tax exemption was availed.

Facts:

X Rural Bank and Y Rural Bank are the constituent banks in a Plan of Consolidation Agreement and Articles of Consolidation. The constituent banks did not previously avail of or enjoy the five-year tax exemption granted under RA No. 7353 or the Rural Banks Act of 1992. The consolidated bank, Z Rural Bank, was issued a Certificate of Authority to operate as a rural bank under RA No. 7353.

Issue:

Is Z Rural Bank, a bank formed through consolidation, entitled to tax exemption under RA No. 7353?

Ruling:

Yes. Rural banks created and organized under the provisions of RA No. 7353 are exempt from the payment of all taxes, fees and charges (except corporate income tax and local taxes) for a period of five years from the date of commencement of operations. Rural banks formed through consolidation may still enjoy the tax exemption for the entire period of five years from the date of commencement of operations in case any or both of the constituent banks did not avail this exemption, or for the remaining period in case the tax exemption was availed.

BIR Issuances

RMC No. 42-2017 circularizes the revised BIR Form No. 2305, or the Certificate of Update of Exemption of Employer and Employee's Information.

RMC No. 42-2017 issued on 14 June 2017

- ▶ BIR Form No. 2305, or the Certificate of Update of Exemption of Employer and Employee's Information, has been revised to reflect the provisions of Revenue Regulations (RR) No. 5-2017, implementing Republic Act (RA) No. 10754 titled "An Act Expanding the Benefits and Privileges of Persons with Disability (PWD)."
- ▶ The revised form updates the portions pertaining to the civil status, employer's information, and additional exemptions, which will now include PWDs as a qualified dependent of a benefactor.

RMC No. 43-2017 announces the availability of new versions of the UEE Data Entry Module that is used in filing BIR Form No. 2305.

RMC No. 43-2017 issued on 14 June 2017

- ▶ The updated version of the UEE Data Entry Module and Batch File, which is used in filing BIR Form No. 2305, now includes a qualified PWD as a dependent for purposes of claiming additional exemptions.
- ▶ The following procedure shall be followed to allow the data entry of a qualified PWD as a dependent for purposes of claiming additional exemptions:
 1. In Part III - Additional Exemptions of BIR Form No. 2305, encode the name and birthdate of the qualified PWD dependent.
 2. Tick the "Mark if PWD/Mentally/Physically Incapacitated" box.
 3. Click the save button after encoding all the required information.
- ▶ Each taxpayer/benefactor can only claim up to four qualified dependent children and/or PWD.
- ▶ Every employer should ascertain whether the PWD, regardless of age, possesses the following qualifications in order to qualify as a dependent of a benefactor:
 1. The PWD must be a Filipino citizen.
 2. He or she must be within the 4th civil degree of consanguinity or affinity of the taxpayer/benefactor.
 3. He or she must not be gainfully employed.
 4. He or she must be chiefly dependent upon and living with the taxpayer/benefactor.

- ▶ The qualified PWD must submit the following documents to their employers during the first year of claiming the exemption and, then, after three years or upon renewal of the PWD ID, whichever comes first:
 1. Duly-accomplished BIR Form No. 2305.
 2. Photocopy of PWD ID.
 3. Sworn Declaration/Identification of Qualified Dependent PWD, Support and Relationship.
 4. Birth Certificate of PWD.
 5. Medical Certificate attesting to the disability duly issued and attested in accordance with the Implementing Rules and Regulations of RA No. 10754.
 6. Barangay Certification attesting to the fact that the PWD is living with the benefactor.

RMC No. 45-2017 publishes the full text of EO No. 19 dated 27 April 2017, titled "Reduction and Condonation of Real Property Taxes and Interests/ Penalties Assessed on the Power Generation Facilities of IPPs under Build-Operate Transfer Contracts with GOCCs".

RMC No. 45-2017 issued on 20 June 2017

- ▶ Section 234 of the Local Government Code (LGC) provides that GOCCs engaged in the generation and transmission of electricity enjoy exemptions/privileges on real property taxes for all machinery and equipment that are actually, directly and exclusively used in the generation and transmission of electric power, including those used for pollution control and environmental protection.
- ▶ LGUs have taken the position that the independent power producers (IPPs) operating within their territories, which are not GOCCs, are not entitled to the above exemptions/privileges of GOCCs.
- ▶ However, considering that a substantial part of the real property taxes charged against the affected IPPs have been contractually assumed by GOCCs, such as the National Power Corporation and the Power Sector Assets and Liabilities Management, payment of such taxes will trigger massive direct liabilities on them, threatening their financial stability, the government's fiscal consolidation efforts, the stability of energy prices, and significant economic losses across all sectors.
- ▶ Given the above scenario, the President has reduced all liabilities for real property tax, including any special levies to the Special Education Fund, assessed by LGUs and other entities for the years 2015 and 2016, on property, machinery and equipment, actually and directly used by IPPs, for the production of electricity under the Build-Operate-Transfer and similar contracts with GOCCs, such as Power Purchase Agreements, Energy Conversion Agreements, and other contractual agreements.
- ▶ The reduced amount shall be equivalent to the tax due computed based on an assessment level of 15% of the fair market value of the property, machinery and equipment depreciated at the rate of 2% per annum, less any amounts already paid by the IPPs.
- ▶ All interest on such deficiency real property tax liabilities are also condoned and the concerned IPPs are relieved from their payment.

- ▶ If the IPPs paid real property taxes in excess of the reduced amount, such excess shall be applied to their real property tax liability for the succeeding years.

BSP Issuances

Circular No. 961 provides for Amendments to the Manual of Regulations for Banks and Non-Bank Financial Institutions as of 31 December 2016.

BSP Circular No. 961 dated 2 June 2017

- ▶ The following statement is added as a footnote to Subsections X409.2/4409Q.2.e., X601.5 / 4601Q.5, X601.6 / 4601Q.6 and Appendices 78/ Q-47 and 78a/ Q-47a:

“The Monetary Board, in its Resolution No. 1945 dated 27 October 2016, approved the discontinuance of access of trust entities to the Bangko Sentral deposit facilities. Trust entities shall no longer have outstanding placement in the Overnight Deposit Facility (ODF) and Term Deposit Facility (TDF) by 30 June 2017.”

- ▶ The phrase “as provided in Item “I” of this Guidelines” under Item “F.g.” of Appendix 108 is hereby deleted.
- ▶ The Sections and Subsections of the Pawnshop Regulations as enumerated under Annex A of this Circular are hereby renumbered to make it consistent with the formatting convention of the Manuals.

[Editor’s Note: Circular 961 was published in The Philippine Star on 14 June 2017]

Circular No. 962 provides for the Guidelines on the Method of Determining Compliance with the Required Basic Security Deposit During the Transition Period* of Spun-off Trust Departments to Trust Corporations.

BSP Circular No. 962 dated 8 June 2017

- ▶ The Circular provides for the amendment of Section 4905T of the Manual of Regulations for Non-Bank Financial Institutions-T Regulations (MORNBFIT) on the transitory provision providing the method of determining compliance with the required basic security deposit during the transition period of spun-off Trust Departments to Trust Corporations.
- ▶ Section 4905T of the MORNBFIT Regulations is hereby amended to add Subsection 4905T.1 to read as follows:

“Subsection 4905T.1 Compliance with the required basic security deposit during and after transition period.

1. During transition period

- ▶ A spun-off trust department shall maintain a basic security deposit equivalent to 1% of its previous end-of-day balance of total trust, investment management, and other fiduciary assets;
- ▶ The newly established trust corporation shall maintain a basic security deposit equivalent to the higher of P500,000.00 or 0.05% of the previous end-of-day balance of total trust, investment management, and other fiduciary assets; and

* The period where both the trust department and trust corporation simultaneously operate for smooth transfer of business operation.

- ▶ A weekly report on the daily compliance with the required basic security deposit shall be submitted to the Bangko Sentral ng Pilipinas (BSP) by the first business day following the reference calendar week (Monday to Sunday).

2. After the transition period

- ▶ The newly established trust corporation shall maintain a basic security deposit equivalent to the higher of P500,000.00 or 0.05% of the balance of the total trust, investment management, and other fiduciary assets as of the end of transition period until one calendar quarter of operations; and
- ▶ Thereafter, the trust corporation shall maintain the required basic security deposit under Subsection 4112T.3 of the MORNBFIT.

The trustee or fiduciary shall have 10 calendar days after the end of day from the start of the transition period until one calendar quarter of operation after end of the transition period within which to deposit with the BSP the additional securities to comply with the required securities.

- ▶ This Circular shall take effect 15 days following its publication in the Official Gazette or in any newspaper of general circulation in the Philippines.

[Editor's Note: BSP Circular No. 962, s. 2017 was published in BusinessWorld on 15 June 2017]

SEC Issuance

SEC-OGC Opinion No. 17-05 dated 8 June 2017

An online English tutorial and diving school that offers its courses for a fee, and thereafter, issues a Diploma or Certificate for Program Completion is considered an educational institution subject to the nationality restrictions under the Constitution.

Facts:

N Corp. is a foreign corporation that seeks to establish a Philippine subsidiary that will operate an online-based English tutorial and diving school which would cater to foreign nationals outside of the Philippines. The Philippine subsidiary would be wholly-owned by N Corp. but majority of its board of directors would be Filipino citizens.

Issue:

Is an online tutorial school exempt from the 60%-40% Filipino-foreign equity requirement under the Constitution?

Held:

An English tutorial program/course, offered to the public to which a diploma or certificate of completion is given thereafter, is considered technical vocational education that can only be offered by a duly-incorporated stock or non-stock educational institution as prescribed under *Batas Pambansa Bldg. 232* or *The Educational Act of 1982*. Technical or vocational schools are within the regulatory power of the Technical Education and Skills Development Authority or TESDA. In an *Opinion* rendered by TESDA to SEC, it made a distinction between two types of vocational schools offering English tutorial courses/programs for purposes of determining whether or not the school is an educational institution under TESDA's jurisdiction:

- a. If a domestic corporation purely caters to foreign clients abroad through on-line tutorial class instruction for a fee and does not issue any Certificate of Training or Diploma for Program Completion, it cannot be considered as engaged in formal technical vocational education or training activities, and hence, not under TESDA's jurisdiction.
- b. If the domestic corporation offers English program for a fee and at the end of the training program will issue any Certificate of Training or Diploma for Program Completion to its successful students, it is considered engaged in formal technical vocational education, regardless of whether the same is performed online or within a regular classroom atmosphere and regardless of whether its students are foreigners or not, and hence, under TESDA's jurisdiction.

Based on the above standards, the SEC held that a corporation engaged in the business of providing formal technical vocational education or training program is an educational institution that must comply with the 60%-40% Filipino-foreign equity requirement under the Constitution.

(N Corp., however, did not mention if the Philippine subsidiary will be issuing diplomas or certificates of completion to its successful students. Since the facts given by N Corp. are insufficient, the SEC did not issue a categorical opinion on N Corp.'s inquiry).

BOC Issuance

CMO No. 13-2017 provides for the Standard Operating Procedure in the Usage and Handling of Weapons of Mass Destruction - Proliferation Prevention Program Provided Equipment under the National Coast Watch System and Conduct of Operation in the Detection, Interdiction and Control of Radioactive Materials.

Customs Memorandum Order No. 13-2017 dated 20 June 2017

- ▶ The guidelines apply to all containerized and non-containerized cargo, conveyance, warehouse and/or person subject to the Bureau of Customs (BOC) jurisdiction.
- ▶ Definitions:
 1. National Coast Watch System (NCWS) refers to an inter-agency mechanism formed under Executive Order (EO) No. 57 to achieve a coordinated and coherent approach to maritime border security, issues and safeguards.
 2. National Coast Watch Council (NCWC) refers to the central inter-agency body tasked with the formulation of strategic direction and policy guidance for the NCWS.
 3. Weapons of Mass Destruction (WMD) refer to any radiological, chemical, biological or other weapon that can kill and bring significant harm to a large number of humans or cause great damage to human-made structures (e.g. buildings), natural structures (e.g. mountains) , or the biosphere.
 4. Proliferation Prevention Program (PPP) refers to an initiative to preclude the illegal propagation and/or spread of WMD, its agents, and/or related precursor materials.
 5. Positive Alarm refers to the radiation above accepted levels on a target as detected by the WMD-PPP provided equipment.

- ▶ Operational procedures provide for the following:
 1. Pre-detection - initial profiling by assigned Customs Officer or Agent of the target cargo, conveyance, warehouse and/or person/s to determine background, declaration of contents, conditions and capability of emitting radioactive signals, whether the same is a norm, legally transported radioactive shipments (e.g., medical isotopes), and/or persons who recently received radio isotopes for medical diagnostics or treatment purposes.
 2. Primary and Secondary Confirmation - When a positive alarm is raised on secondary confirmation, and when the target is not covered by any valid permit, clearance, authority or registration and/or license, the BOC shall cause the physical isolation, detention, security and storage of the target cargo, conveyance, warehouse and/or person/s based on accepted and safe handling measures pending disposition, seizure and/or forfeiture proceedings.
- ▶ The following are the grounds for immediate detainment:
 1. Discovery of a neutron source or plutonium or uranium;
 2. Unidentified point-source radiation;
 3. Inexplicably high levels of radiation;
 4. Suspicious isotope;
 5. Isotope identified does not match the shipping documentation.
- ▶ The CMO provides for reportorial requirements by the BOC to the NCWC regarding the detection of contraband/s under the WMD-PPP provided equipment and on negative alarm/confirmation, report in detail of the negative findings to the concerned District Collector and/or Customs Commissioner together with appropriate recommendations.
- ▶ This CMO shall take effect immediately.

[Editor's Note: CMO No. 13-2017 was received by the UP Law Center on 27 June 2017]

PEZA Update

PEZA Memorandum Order No. 2017-21 circularizes the roll-out of the PEZA e-Payment System, an application which allows locators to pay PEZA fees online.

PEZA Memorandum Circular No. 2017-021 dated 29 May 2017

- I. Background
 - ▶ PEZA e-Payment System (PEPS) aims to make all fee payments more convenient for PEZA clients
 - ▶ Roll-out: 1 June 2017

II. PEZA e-Payment System

- ▶ PEPS is a payment gateway facility of PEZA that enables registered locators and accredited brokers to process their payments online
 1. Modes of payment: ATM card, debit card, e-wallet
 2. Available 24/7 nationwide
 3. Payer's copy of the e-Official Receipt (e-OR) is sent thru email or SMS
 4. E-payment transaction information is transmitted to the collecting officer in the zone/unit processing the requested transaction
 - ▶ For e-Import Permit / Automated Export Declaration, the payer company must alert the collecting officer (SEZ) / Head Office finance officer (for JPCO) and submit via email an accomplished e-Permit Advance Payment Form as basis for posting in the VASP's ledger
 5. Service provider will charge a PHP 35 processing fee for transactions using ATM, Debit Card and e-Wallet, plus 2% additional charge per transaction for transactions using local credit cards
- ▶ Website access: epay.peza.gov.ph

BOI Updates

BOI Memorandum Circular No. 2017-004 provides the general policies and specific guidelines for the registration of projects and availment of incentives under the 2017 IPP.

Memorandum Circular No. 2017-004 dated 14 June 2017

I. Background

- ▶ The 2017 Investment Priorities Plan (IPP) was approved by the President through Memorandum Order No. 12 dated 28 February 2017.
- ▶ The 2017 IPP is a rolling three-year plan, the specific criteria and qualifications for registration/incentives under which are clarified in the General Policies and Specific Guidelines issued by the Board of Investments (BOI).

II. Salient Provisions and Key Changes from the 2014 IPP

- ▶ The 2017 IPP identified three additional preferred activities: (i) Innovation Drivers, (ii) Inclusive Business Models, and (iii) Environment or Climate Change-Related Projects.
- ▶ Priority strategic services now include telecommunications and state-of-the-art engineering, procurement and construction projects.
- ▶ The price ceiling for mass housing projects was adjusted from PHP 3 Million to PHP 2 Million.

- ▶ By year 2020, contact centers and non-voice business processing activities locating in Metro Manila may no longer be qualified for incentives availment with the BOI under E.O. No. 226.
- ▶ Minimum investment cost requirement for contact centers reduced from USD 5,000 per seat to USD 2,500 per seat.
- ▶ Allowance for Capital Equipment to Labor Ratio as an ITH bonus criteria increased to 1 direct employee is to USD 28,000 (from previous 1 direct employee is to USD 10,000).
- ▶ Coverage of registrable manufacturing projects expanded to broadly include more manufacturing activities.

III. General Policies

- ▶ Approval of Application and Entitlement to Incentives
 1. Approval for registration shall be based on the IPP listing
- ▶ Equity ownership
 1. No restrictions on foreign ownership for export-oriented and/or pioneer enterprises that will engage in the activities listed in the IPP, except as provided in the Constitution and Foreign Investments Act of 1991.
- ▶ Geographical considerations in industry development policy
 1. Projects in any of the identified Less Developed Areas (LDAs) shall be entitled to pioneer incentives and additional deduction from taxable income equivalent to 100% of expenses incurred in the development of necessary and major infrastructure facilities.
 2. Projects in NCR are not entitled to Income Tax Holiday, but exemption from the locational restriction may be given to:
 - ▶ Projects in government industrial estates;
 - ▶ Projects that will engage in service type activities.

BUT: Contact centers and non-voice business processing activities that will be located in Metro Manila may no longer be qualified for incentives availment with the BOI under E.O. No. 226 by year 2020

 - ▶ Expansion of export-oriented projects effected within the firm's existing premises;
 - ▶ Modernization projects.
- ▶ ITH availment
 1. General Rule: Income qualified for ITH shall be limited to the income directly attributable to the eligible revenue generated from the registered project

2. Base Figure and Rate of Exemption:

- ▶ ITH availment of expansion projects is subject to a base-figure equivalent to the enterprise's highest sales volume/value in the last three years prior to the start of commercial operations of the project.
- ▶ Projects registered under modernization program without increase in capacity may be entitled to three years ITH and other incentives.

3. Availment of ITH Bonus Year:

- ▶ Capital Equipment to Labor Ratio criterion: USD 28,000 in capital equipment is to 1 direct employee.
 - ▶ Net Foreign Exchange Earnings/Savings criterion: At least USD 500,000 for the first three years of commercial operations.
 - ▶ Indigenous Raw Materials Cost criterion: At least 50% of total input.
- ▶ Multi-phase projects
1. Projects with multiple phases/locations may be registered on a per phase/location basis.
- ▶ Equipment
1. Registered enterprises shall use brand new equipment, except: (i) projects utilizing consigned equipment, (ii) projects involving transfer of facilities, (iii) when specified in the Specific Guidelines, (iv) strategic projects/considerations as determined by the Board, (v) projects which will apply production processes that meet environmental standards.

IV. Specific Guidelines

A. Preferred Activities

- ▶ All Qualified Manufacturing Activities including Agro-Processing
 1. Manufacture of industrial goods.
 2. Processing of agricultural and fishery products, including Halal and Kosher food into semi-finished/intermediate goods for use as input or finished products for final consumption.
 3. Manufacture of modular housing components and machinery and equipment, including parts and components:
 - ▶ Projects must utilize up-to-date and market-appropriate technology, and must comply with the Philippine National Standards (PNS);

- ▶ To be qualified for registration, must also satisfy any of the following criteria:
 - a. Will manufacture/process products, the importation of which grew by an annual average of at least 10% from 2012-2016, or the share of imports to total apparent demand is at least 60%; or
 - b. The project's value creation is at least 50%, except for consumer durables and industrial products or their intermediate goods that should be at least 25%; or
 - c. Will manufacture/process products that will utilize new technology and/or work-class designs; or
 - d. The project has a core capital equipment cost to direct labor ratio of not higher than \$28,000:1 worker at full capacity; or
 - e. Will adhere to Halal or Kosher standards for food manufacturing, as accredited by the PAB.
- ▶ Except for modernization projects, only projects located outside Metro Manila may qualify for registration.
- ▶ Agriculture, Fishery and Forestry
 1. Commercial production of agricultural, fishery and forestry products.
 2. Production of seeds and seedlings.
 3. Establishment of nurseries and hatcheries:
 - ▶ Support services and infrastructures such as facilities for drying, cold chain storage, blast freezing, bulk handling and storage, harvesting, plowing, spraying and dusting, packing houses, trading centers, ice plants in less developed areas, AAA slaughterhouses, and AAA dressing plants.
 - ▶ Except for modernization projects, only projects located outside Metro Manila may qualify for registration.
 - ▶ Modernization projects include those for agricultural support services and infrastructure only.
- ▶ Strategic Services
 - ▶ Integrated circuit design
 1. Covers all logic and circuit design techniques required to design ICs.

- ▶ Creative industries / knowledge-based services
 2. IT business process management for the domestic market (e.g. contact centers, artificial intelligence, data science/ analytics services, back-offices services, IT services, creative services, other non-voice services).
 3. Services involving original content (e.g. animation, software development, game development, health information management systems, and engineering design).
 4. Digital or technological start-ups/activities
 - ▶ Upgrading of existing or baseline skills/training program related to people, process, tools, and technology to a higher level of certification or standards may qualify for registration as a modernization project.
- ▶ Maintenance, repair and overhaul (MRO) of all types of aircraft.
- ▶ Charging/refueling stations for alternative energy vehicles, except LPG-run vehicles.
- ▶ Industrial Waste Treatment
 1. Establishment of treatment facilities for toxic and hazardous waste (THW) from an industrial operation.
 - ▶ The following are the qualifications for registration:
 - i. Must involve treatment, storage and disposal (TSD);
 - ii. Must be capable of handling THW; and
 - iii. Must handle only locally generated industrial wastes.
- ▶ Telecommunications
 1. Establishment of connectivity facilities for fixed and mobile broadband services.
 2. Registration limited to new players only.
- ▶ State-of-the-art engineering, procurement, and construction (EPC)
 1. Covers engineering, design, procurement, and construction for industrial plants and infrastructure.
- ▶ Healthcare Services, including Drug Rehabilitation Centers
 1. Establishment and operation of general and specialty hospitals, and other medical/healthcare facilities.
 - ▶ Any of the following may qualify for registration:
 - a. General Hospitals (Level 1, 2, and 3) in specified locations

- b. Specialty Hospitals located outside Metro Manila
- c. Other Medical/Healthcare Facilities located outside Metro Manila:
 - ▶ Custodial Care Facilities including geriatric care and drug rehabilitation centers
 - ▶ Diagnostic/Therapeutic Facilities (excluding Clinical Laboratory, Drug Testing Laboratory, Laboratory for Drinking Water Analysis), and
 - ▶ Specialized Out-Patient Facilities (excluding In-Vitro Fertilization Center and Stem Cell Facility)
- ▶ Only revenues derived from medical and diagnostic services rendered by the registered entity shall be entitled to ITH.
- ▶ Income from lease/rent, and revenues from any other non-treatment related services will not be eligible for ITH.
- ▶ Mass Housing
 1. Economic and low cost housing
 - ▶ The following are the qualifications for registration:
 - a. The selling price of each housing unit shall be more than PHP 450,000.00 but not exceeding PHP 2.0 million;
 - b. The project must be located outside Metro Manila;
 - c. Minimum of 20 livable dwelling units in a single site or building;
 - d. Must be new or expanding economic/low-cost housing project;
 - e. For residential condominium projects, at least 51% of the total gross floor area must be devoted to housing units.
 2. All economic/low-cost housing projects must comply with the socialized housing requirement (SHR) by building socialized housing units in an area equivalent to at least 20% of the total registered project area or total BOI registered project cost for subdivision housing and 20% of the total floor area of qualified saleable housing units for residential condominium projects.
 3. Only projects located outside Metro Manila may qualify for registration.
 4. In-city low-cost housing projects for lease
 - ▶ Covers newly constructed, low to medium-rise dormitory type housing projects, including those located in Metro Manila

- a. The following are the qualifications for registration:
 - ▶ Minimum of 20 livable dwelling units for lease in a single building;
 - ▶ Within 4 kilometer radius from an economic zone, industrial parks/complex or business districts; and
 - ▶ Monthly lease price shall not exceed the threshold of the Rent Control Act (R.A. No. 9653) covering all private residential units with monthly rent of PHP 10,000.00.
 - b. Registered enterprises shall not be required to comply with the SHR.
- ▶ Infrastructure and Logistics, including Local Government Unit Public-Private Partnership (LGU-PPP) Projects
 1. Establishment and operation of physical infrastructures vital to the country's economic development and prosperity.
 2. PPP projects, including those initiated/implemented by LGUs.
 - ▶ Airports and seaports (including RO-RO ports) for cargo and passenger
 - a. Qualification shall be based on government's infrastructure development policy.
 - ▶ Air, land, and water transport
 - a. Air transport
 - ▶ Passenger and/or cargo air transport operation for commercial purposes
 - i. Only revenues derived from cargo air freight fares, passenger air fares, and revenues on refund, cancellation, and rebooking fees shall be entitled to ITH;
 - ii. Incidental revenues (e.g. excess/prepaid baggage, seat selector options, merchandise sales) shall not be entitled
- ▶ Land mass transport
 - a. Mass transport using brand new buses that run on electric battery and/or compressed/liquefied natural gas.
 - b. Public utility vehicles (PUVs) as defined by DOTr, LTFRB, and LTO as part of the PUV Modernization Program.

- ▶ Water transport
 - a. Domestic/inter-island shipping, i.e. pure cargo, passenger, and passenger-cargo vessel operations (including RORO, ROPax, Ferry Terminal System operations and overseas shipping).
 - b. Tanker, high-speed craft, RORO vessels serving primary routes and passenger/cargo vehicles having a gross weight of 150GT and above.
 - c. Small passenger vessels such as ferry boats serving small islands/inland water/missionary routes.
 - ▶ The following are the qualifications for registration for overseas shipping:
 - i. Must be a Philippine shipping enterprise accredited with the MARINA;
 - ii. Vessel must be registered and operated under the Philippine flag; and
 - iii. Vessels must be at least 1,000 GT.
 - ▶ Upgrading of skills for crew complements of passenger vessels to international standards may qualify for registration as modernization project.
- ▶ Mass rail
 - a. Mass rail transport system for passengers and cargo in line with the transport development plans of DOTr and DOST.
- ▶ Liquefied natural gas (LNG) storage and regasification facilities
 - a. Establishment and operation of natural gas storage and regasification facilities.
- ▶ The following are the qualifications for registration:
 - i. Must have new facilities;
 - ii. Must cater to power plants, industrial plants, commercial establishment, etc.; and
 - iii. Must cater to at least 1 clientele, other than the proponent's own business.
- ▶ Pipeline projects for oil and gas
 - a. Establishment of a new pipeline facility for transport of petroleum products and natural gas, petrochemical and similar products.

- ▶ Bulk water treatment and supply
 - a. Must involve extraction of water from its natural source (except shallow and deep wells), and water treatment for commercial purposes.
 - b. Only new bulk water and supply facilities may qualify for registration.

- ▶ Training facilities
 - a. Establishment and operation of training and learning facilities specializing in developing skills in technical, vocational education and training in support of the activities listed in the 2017 IPP.
 - ▶ The following are the requirements for registration:
 - i. The curriculum must be approved by either TESDA for training courses or CHED for degree courses; and
 - ii. The registered education/training/learning institutions must have laboratory/s, equipment and tools for training.

- ▶ Testing laboratories

- ▶ Domestic industrial zones
 - a. Development of domestic industrial zones outside Metro Manila.
 - ▶ The following are the requirements for the zone:
 - i. Minimum area of 20 hectares of contiguous land;
 - ii. Has core infrastructure/facilities such as paved roads, power system, water supply, drainage system, pollution control devices and communications facilities;
 - iii. Has at least 5 locators; and
 - iv. Development must be completed within a maximum period of three years from registration.

- ▶ PPP projects
 - a. Projects implemented under R.A. No. 6957, as amended by R.A. No. 7718 (Amended Build-Operate-Transfer Law), including those initiated/implemented by LGU.

- ▶ Tollways
 - a. Development and/or operation of tollways
 - ▶ Both the developer and operator may qualify for registration, if the development and operation are undertaken by separate entities.

- ▶ Innovation Drivers
 - a. Research and development (R&D) activities
 - ▶ All R&D activities;
 - ▶ Establishment and operation of facilities for conduct of clinical trials (e.g. Contract Research Organization).

 - b. Centers of Excellence
 - ▶ Establishment of institutions specializing in technical education and training in various disciplines.

 - c. Innovation Centers, Business Incubation Hubs, and Fabrication Laboratories/Co-working Spaces
 - ▶ Covers support services and infrastructures for MSMEs through the use of office space, machinery and equipment, and/or provision of technical/business counselling assistance.
 - ▶ Innovation Center - Communities of industry entrepreneurs and academic researchers, as well as mandated government agencies, working in partnership to find breakthroughs and alternative solutions to address current industry challenges.
 - ▶ Business Incubation Hubs - Assists entrepreneurs and startup companies develop a repeatable and scalable business model by providing infrastructure and services.
 - i. Must have the following facilities: office space, internet access, business meeting/conference room, training room, storage room.
 - ii. Must provide the following services:
 - ▶ technical assistance;
 - ▶ intellectual property management;
 - ▶ business development and marketing assistance;
 - ▶ administrative services.
 - ▶ FabLabs - Computer-based innovation, design, and fabrication workshops with the aim of developing or building models of new products and prototypes.

- ii. At least 300 farmers/fisherfolk/suppliers/individual beneficiaries engaged, of which, at least 30% are women;
 - iii. At least 20% increase in average income of individuals engaged from MSEs, cooperatives or any organized entity duly recognized by a government body from the baseline year to the third year of actual operation; and
 - iv. Exhibits innovation in the business model through:
 - ▶ Provision of technical assistance/capacity building to MSEs and/or individual farmers and fisherfolk that increases productivity and/or quality;
 - ▶ Facilitation of access to finance; or
 - ▶ Provision of inputs and/or technology to MSEs and/or individual farmers and fisherfolk that would increase productivity or improve product quality.
- ▶ Qualified tourism enterprises shall target and accomplish all of the following within three years of commercial operation:
- i. At least 25% of total cost of goods/services sold are sourced from MSEs At least 25 direct jobs (regular employment) generated for individuals in the identified databases, of which, at least 30% are women;
 - ii. At least 20% increase in average income of individuals engaged from MSEs, cooperatives or any organized entity duly recognized by a government body from the baseline year to the third year of actual operation; and
 - iii. Exhibits innovation in the business model through:
 - ▶ Provision of technical assistance/capacity building to MSEs and/or the direct jobs generated that increases productivity/quality or addresses specific knowledge gaps needed for the job;
 - ▶ Facilitation of access to finance.
- ▶ A BOI-registered New project engaged in agri-business or tourism activity may qualify for upgrade to pioneer status and be entitled to another year of ITH if it intends to undertake IB model, provided that:
- i. The registered project has yet to avail of the ITH or is within its first three years of ITH entitlement period;
 - ii. The registered enterprise has filed the request for upgrade to pioneer status within 12 months from the effectivity of this Guidelines;
 - iii. The registered enterprise will accomplish/has accomplished the requirements for IB model enumerated above.

- ▶ Environment or Climate Change-Related Projects
 - a. Manufacture/assembly of goods
 - b. Establishment of energy efficiency-related facilities, which would lead to (i) efficient use of energy, natural resources, or raw materials, (ii) minimize/prevent pollution, or (iii) reduce greenhouse gas emissions.
 - c. Green ship recycling
 - d. Establishment of privately-owned materials recovery facility.

- ▶ Energy
 - a. Covers power generation projects utilizing conventional fuels, waste heat and other wastes.
 - b. Establishment of battery energy storage systems:
 - ▶ Coal-fired power plants must utilize at least the super critical boiler technology or its equivalent in terms of emissions;
 - ▶ Modernization of coal-fired power plants that will convert to at least a super critical boiler technology or its equivalent in terms of emissions including its turbine or generator may qualify for registration;
 - ▶ To qualify for registration, diesel and bunker-fired power projects shall be integrated with renewable energy (hybrid power systems) or providing ancillary power services as contingency reserve;
 - ▶ Revenue from sales of electricity sourced from the Wholesale Electricity Spot Market (WESM) shall not be entitled to ITH;
 - ▶ Within two years from the date of registration, projects with loan components in their financing scheme must have achieved financial close;
 - ▶ Projects should utilize energy sources adopting environmentally-friendly technologies that comply with relevant environmental laws.

B. Export Activities

- ▶ Production and manufacture of export products
 1. Covers the production/manufacture of non-traditional export products.
 2. Export requirement: At least 50% of total output if Filipino-owned, or at least 70% if foreign-owned.

- ▶ Services exports
 1. Service activities rendered to clients abroad and paid for in foreign currency.
 2. Non-voice business processing operations, such as administrative and business services including analytics, data management, engineering and architectural services.
 3. Export requirement: At least 50% of revenue if Filipino-owned, or at least 70% if foreign-owned.
 4. For contact centers, project must have a minimum investment cost of the Philippine Peso equivalent of USD 2,500 per seat to qualify for registration.
 5. Upgrading of existing or baseline skills/training program related to people, process, tools and technology to a higher level of certification or standards may qualify for registration as modernization project.

- ▶ Activities in support of exporters
 1. Activities directly supporting export producers, as follows:
 - ▶ Manufacture of parts/components and materials and supplies directly/ reasonably needed in the production of the export product;
 - ▶ Services comprising a portion of the manufacturing process;
 - ▶ Product testing and inspection;
 - ▶ Repair and maintenance; and
 - ▶ Logistics services.
 2. Service providers to foreign film and television production projects in the country.

C. Special Laws

- ▶ Industrial Tree Plantation
 1. Covers extensive plantation of timber, non-timber species and fruit trees for commercial and industrial purposes.

- ▶ Mining - Limited to capital equipment incentive
 1. Exploration and development of mineral resources, mining/ quarrying and processing of metallic and non-metallic minerals.
 2. The following may qualify for registration:
 - ▶ Exploration of mineral resources;

- ▶ Processing of metallic and non-metallic minerals to produce semi-processed mineral products, e.g. metallic ore concentrate, whether or not integrated with mining/quarrying operations.
- 3. Production of pure metals, whether or not integrated with mining operations, shall be covered under manufacturing.
- 4. Mere mining/quarrying or even those with minimal processing (e.g. crushing, grinding, screening, drying) shall not qualify for registration.
- ▶ Publication or Printing of Books/Textbooks
 1. Content development intended for books
 2. Publication of books in print or digital format
 - ▶ The following may qualify as new:
 - a. New book titles (original works, and original text with annotations, with ISBN), and
 - b. First format by which the new book title will be produced or published. The succeeding format (e.g., print to digital, or vice versa) by which the same title is published will be regarded as "Expansion."
 - ▶ Re-prints, revisions, and succeeding editions of existing titles will not qualify for registration.
 - ▶ For publishing, the following will apply:
 - a. A minimum of 3 titles with 500 copies each for its first print run, in case of trade books;
 - b. A minimum of 3 titles with 1,000 copies each for its first print run, in case of printed text-books; and
 - c. A minimum of 3 titles each, in case of e-books.
- ▶ Refining, Storage, Marketing and Distribution of Petroleum Products
 1. Refining, storage, distribution, and marketing of petroleum products.
 2. For gasoline retailing stations, the applicant shall be required to invest a minimum capital of PHP 10 million per station (excluding land).
 3. For storage, marketing and distribution, only investments of new industry participants may be entitled to incentive.
 4. Blending of petroleum products alone may only be entitled to capital equipment and other non-fiscal incentives.

- ▶ Rehabilitation, Self-Development and Self-Reliance of Persons with Disability
 1. Manufacture of technical aids and appliances for the use and/or rehabilitation of persons with disability.
 2. Establishment of special schools, day care centers, homes, residential communities or retirement villages solely to suit the needs and requirements of persons with disability.

- ▶ Renewable Energy
 1. Developers of renewable energy facilities, including hybrid systems.
 2. Manufacturers, fabricators and suppliers of locally-produced renewable energy (RE) equipment and components.

- ▶ Tourism
 1. Tourism enterprises that are outside the tourism enterprise zones (TEZs).
 2. Tourist transport services whether for land, sea and air transport for tourist use.
 3. Establishment and operation of:
 - ▶ Accommodation establishments: hotel, resort, apartment hotel/serviced residences, guest accommodation, eco-lodge, and homestay;
 - ▶ Convention and exhibition facilities or “meetings, incentives, conventions and exhibition” (MICE) facilities;
 - ▶ Amusement parks;
 - ▶ Adventure and eco-tourism facilities;
 - ▶ Sports facilities and recreational centers;
 - ▶ Theme parks;
 - ▶ Health and wellness facilities such as but not limited to spas;
 - ▶ Farm tourism; and
 - ▶ Tourism training centers and institutes.
 4. Development of retirement villages.
 5. Restoration/ preservation and operation of historical shrines, landmarks and structures.

[Editor's Note: Published in The Philippine Star on 18 June 2017, page B6]

DTI-BOI Administrative Order No. 1 provides the implementing guidelines of EO No. 22, which extends for another year the duty-free incentive for importations of capital equipment and machinery, spare parts, and accessories of BOI-registered entities.

DTI-BOI Administrative Order No. 01 s2017 dated 31 May 2017

- ▶ Executive Order (E.O.) No. 22 extends for another year the duty-free incentive for importations of capital equipment and machinery, spare parts, and accessories for BOI-registered entities
- ▶ Coverage: Importations by BOI-registered new and expanding enterprises of capital equipment and machineries, spare parts, and accessories classified under Chapters 40, 59, 68, 69, 70, 73, 76, 82, 83, 84, 85, 86, 87, 89, 90, 91, and 96 of the Customs Modernization and Tariff Act (CMTA)
- ▶ Conditions:
 1. The imported capital equipment, spare parts, and accessories are not manufactured domestically in sufficient quantity, of comparable quality, and at reasonable prices.
 - ▶ To be considered as available in sufficient quantity, it should be made available to the enterprise at the time needed or within a reasonable period.
 - ▶ To determine if quality is comparable, the test, among others, is whether (i) the registered operation will be adversely affected, (ii) the resulting product will be of lower quality, or (iii) the cost of operation will be increased.
 - ▶ To determine reasonableness of prices quoted by domestic manufacturers, BOI may be guided by the acquisition cost if imported (assuming all taxes and duties were paid thereon) plus 15% mark-up.
 2. The imported capital equipment, spare parts, and accessories are reasonably needed and will be used exclusively by the enterprise in its registered activity.
 3. BOI approval for the importation was obtained before the release of shipment by the Bureau of Customs (BOC).
 4. The rated capacity of the capital equipment to be imported, if applicable, is within the registered capacity of the enterprise.
- ▶ Enterprises availing of the 0% duty importation shall submit an application with the BOI.
- ▶ The BOI has 10 working days from official acceptance to act on the application.
- ▶ If the application is approved, the BOI shall issue a Certificate of Authority (CA) for the importations covered under E.O. No. 22.
 1. The CA shall include, among others, the (i) registration number, (ii) type of registration, (iii) date of application, (iv) date of issuance, (v) validity period, (vi) quantity and description of capital equipment, spare parts, and accessories to be imported, and (vii) applicable AHTN tariff code.
 2. The CA is non-transferrable and valid for a period of one year from issue date, unless earlier invalidated or revoked (subject to the effectivity of E.O. No. 22).

- ▶ The enterprise shall submit to DOF the official import documents together with the CA.
- ▶ Upon issuance of the DOF endorsement, the enterprise shall file an import entry declaration with the BOC, along with the supporting documents.
- ▶ The Customs Collector shall verify if the importation is covered by E.O. No. 22.
 1. In case of discrepancy between the tariff classification and result of the inspection, the BOC classification shall prevail.
 2. If BOC classification is nonetheless still covered by E.O. No. 22, 0% may still apply subject to amendment of the CA.
 3. If BOC classification is outside E.O. No. 22, the shipment shall only be released upon payment under protest of the appropriate duty rates and posting of a cash or surety bond.
- ▶ Performance bond
 1. Posting of a performance bond with the Government Service Insurance System (GSIS) equivalent to the duties waived on the importation shall be a pre-condition to 0% duty importation.
 2. In lieu of the bond, the BOI may instead require other forms of guarantee (e.g. guarantee from the principal stockholder/s).
 3. In the event of a violation, the principal stockholder/s shall be solidarily liable with the enterprise.
 4. The performance bond may be lifted: (i) for domestic enterprises, upon installation and utilization of the imported capital equipment for the registered activity; and (ii) for export enterprises, after a period of one year of exportation.
 5. The BOI may waive the performance bond for qualified enterprises with good track record.
- ▶ Monitoring
 1. Within 15 days from release of shipment from customs, the enterprise should give written notice to the BOI and submit copies of the Import Entry and Internal Revenue Declaration (IEIRD).
 2. Within 10 days from installation of the equipment in the site, the enterprise should likewise inform the BOI.
 3. The BOI may inspect the enterprise's site to verify whether the capital equipment has indeed been installed and is being used in the registered activity.
- ▶ Sale or disposition
 1. Any sale, transfer, assignment, donation, or other form of disposition within five years from acquisition shall require prior BOI approval.

2. Approval shall only be granted if the sale or disposition is made:
 - ▶ To another qualified enterprise;
 - ▶ For reason of technical obsolescence as determined by BOI;
 - ▶ For purposes of replacement to improve and/or expand the operations of the enterprise;
 - ▶ Sale, transfer, disposition within the five year period without prior BOI approval shall subject the enterprise and the transferee to solidary liability to pay whichever is higher of twice the amount of foregone taxes or PHP 500,000;
 - ▶ Sale, transfer, disposition after five years from acquisition shall require notice to the BOI within 10 days from such sale, transfer, or disposition.
- ▶ Penalties for violation
 1. Any violation shall result in the suspension of all BOI incentives that are available for a particular project for the taxable year.
 2. Corresponding penalties may also be meted, whenever warranted.
 3. If penalties are not paid, the imported capital equipment shall be confiscated in favor of the government.
 4. Other administrative sanctions may include: (i) cancellation or withdrawal of the CA, (ii) automatic disapproval of pending or subsequent application for CA, (iii) blacklisting.

[Editor's Note: Published in The Philippine Star on 9 June 2017]

BLGF Opinions

BLGF Opinion dated 16 May 2017

Gross receipts realized by a specialty contractor from its overseas construction projects are not subject to local business tax.

Facts:

T Co. is a domestic corporation whose principal classification is for well drilling work. It has no branches or sales outlets, but maintains project offices in different localities in the Philippines. It is also registered as a Specialty Contractor at the Philippine Overseas Construction Board. As part of its business expansion plan, T Co. intends to offer its well drilling and construction services to clients located overseas.

Issue:

Are cities and municipalities authorized to impose and collect local business tax ("LBT") on gross receipts realized by a specialty contractor from its overseas construction projects?

Ruling:

No. Gross receipts must be realized from services rendered within the jurisdiction of the local government imposing tax. Thus, if the services were performed beyond the territorial jurisdiction of the taxing authority, the power to tax may not be exercised.

It is an established principle of taxation that the power to impose a privilege or excise tax upon the exercise or enjoyment of a right or privilege is limited to the territorial jurisdiction of the sovereign, and a state is without jurisdiction to impose a tax on business unless activities which are the subject of the tax are carried on within its territorial limits, irrespective of the place where the party doing business has residence.

BLGF Opinion dated 20 April 2017

Local Economic Enterprises are subject to income tax and VAT.

Facts:

D Co. is a hotel company registered as local economic enterprise (LEE) of the City Government of Dapitan. It has been paying income tax and Value Added Tax (“VAT”) to the Bureau of Internal Revenue (“BIR”). D Co. asserts that, as an LEE, it shall no longer be required to pay income tax and VAT to the BIR, and that all revenues collected by it shall accrue exclusively to the local government of Dapitan.

On the other hand, the BIR contends that D Co. is subject to tax because it is operating as a business.

Issue:

Is D Co. subject to income tax and VAT?

Ruling:

Yes. Any activity of a local government unit (LGU) which is proprietary in nature may be subject to tax.

Section 15 of the Local Government Code (LGC) expounds on the powers of a municipality, which are two-fold in character: as public, governmental or political on one hand, and as corporate, private or proprietary on the other.

Under Section 18 of the LGC, LGUs are authorized to generate their own sources of revenues and the allocation of the same shall accrue exclusively to them. As part of their powers to create sources of revenues, LGUs may venture in the operation of LEE.

Properties of the State and of its municipal subdivisions devoted to government uses and purposes are generally deemed to be exempt from taxation, although no express provision in the law is made therefor. However, the taxability of an economic enterprise shall be resolved by considering the purpose and intent for establishing the said enterprise. Whereas purely governmental function are exempt from taxes, the acts of an LGU in its corporate capacity and for the purpose of economic gain and profit may be subject to tax and treated just like any other private or government corporation.

Section 30 of the National Internal Revenue Code provides that *the income of whatever kind and character of the foregoing organizations from any of their properties, real or personal, or from any of their activities conducted for profit regardless of the disposition made of such income, shall be subject to tax imposed under this Code.*

Even a non-stock, non-profit organization or government entity is liable to pay VAT on the sales of goods and services. As long as the entity provides service for a fee, remuneration or consideration, then the service rendered is subject to VAT.

Considering that the purpose of the creation of LEE is proprietary in nature, D Co. may be subject to tax. To exempt D Co. from taxes imposed by the BIR, it must prove that the objective of its economic endeavor is purely governmental. It must present evidentiary documents, the purpose of its creation, the manner of its operation, intended recipients of its services or customers and the disposition of its revenues.

Court Decisions

Bureau of Internal Revenue, et al vs. Lepanto Ceramics Inc.

Supreme Court First Division, G.R. No. 224764 promulgated 24 April 2017

Where a Rehabilitation Court issues an Order calling for the suspension of the enforcement of claims against a distressed company, the BIR's act of sending a notice of informal conference and Formal Letter of Demand to the distressed company are considered acts of defiance of the Order.

The remedy of the BIR is to submit its claim to the Rehabilitation Court for proper consideration so that it may participate in the proceedings.

Facts:

Lepanto Ceramics Inc. (LCI) filed a petition for corporate rehabilitation pursuant to the Financial Rehabilitation and Insolvency Act of 2010 (or FRIA). In its petition, LCI admitted to the national government its tax liabilities of at least P6 million.

The Rehabilitation Court, Calamba Regional Trial Court (RTC) Branch 34, issued a Commencement Order which declared LCI to be under corporate rehabilitation, suspended all actions or proceedings for the enforcement of claims against LCI, and directed the BIR to file and serve on LCI its comment or opposition to the petition, or its claims against LCI. The BIR was notified personally and by publication of said Order.

Despite the Order, Petitioner Alfredo Misajon, then Assistant Commissioner of the BIR's Large Taxpayer's Service, and Revenue Officers Balbido and Martirez sent LCI a notice of informal conference, and subsequently, a Formal Letter of Demand requiring LCI to pay deficiency taxes for the Fiscal Year ending 30 June 2010 of P567 million.

LCI filed a petition for indirect contempt against the BIR, stating that the actions of Misajon et al. in pursuit of the claims for deficiency taxes despite the Commencement Order violate the Rules of Court, in relation to the FRIA. Misajon et al. argued that their actions were intended to toll the prescriptive period to collect deficiency taxes and that the indirect contempt proceedings interfere with the exercise of their functions to collect taxes due to the government.

RTC Branch 35 ruled in favor of LCI, and stated that Misajon et al.'s acts of sending LCI a notice of informal conference and Formal Letter of Demand are for the purpose of pursuing and enforcing a claim for deficiency taxes, and thus, are in clear defiance of the Commencement Order of the Rehabilitation Court.

Issue:

Was it proper for the BIR to issue the notice for informal conference and Formal Letter of Demand to LCI?

Ruling:

No, the issuances were improper and constituted a defiance of the Commencement Order.

Corporate rehabilitation is an attempt to conserve and administer the assets of an insolvent corporation in the hope of its eventual return from financial stress to solvency. It contemplates the continuance of corporate life and activities in an effort to restore and reinstate the corporation to its former position of successful operation and liquidity.

The purpose of rehabilitation is to find ways and means to minimize the expenses of the distressed corporation during the rehabilitation period by providing the best possible framework for the corporation to gradually regain or achieve a sustainable operating form.

In order to achieve this objective, the law provides that upon the issuance of a Commencement Order, which includes a Stay or Suspension Order, all actions or proceedings, in court or otherwise, for the enforcement of "claims" against the distressed company shall be suspended.

The word "claims" includes those of the government, whether national or local, including taxes, tariffs, and customs duties.

Creditors of the distressed corporation are not without remedy as they may still submit their claims to the rehabilitation court for proper consideration so that they may participate in the proceedings. Any attempt by the creditors to seek legal or other resource against the distressed corporation shall be sufficient to support a finding of indirect contempt of court.

Misajon et al. could have tolled the running of the prescriptive period and at the same time, performed their functions as officers of the BIR without defying the Commencement Order and without violating the laudable purpose of the FRIA by ventilating their claim before the Rehabilitation Court.

The act of sending a notice of a notice of informal conference and a Formal Letter of Demand are part of the process for the assessment and collection of taxes from delinquent taxpayers - an action for the enforcement of a claim which should have been suspended by virtue of the Commencement Order.

Asia United Insurance, Inc. vs. Commissioner of Internal Revenue

CTA (First Division) Case No. 8916, promulgated 17 May 2017

The BIR has a period of five years following the assessment within which to collect the tax from a taxpayer. A request for a reduction, waiver, or compromise of penalties does not suspend the prescriptive period to collect the tax.

Facts:

On 31 January 2006, Petitioner Asia United Insurance, Inc. (Asia United) received from Respondent CIR a Final Assessment Notice (FAN) for alleged deficiency Documentary Stamp Tax (DST) for taxable year 2003. Asia United paid the basic tax due on the deficiency assessment but requested for the abatement of interest and compromise penalties on the ground of financial incapacity. The BIR approved the abatement of the compromise penalty but denied the cancellation of interest. On 18 December 2013, the BIR served a Warrant of Distraint or Levy on Asia United for the interest portion of the deficiency assessment.

Asia United protested the collection proceedings on the ground that the BIR's period to collect has already prescribed. As the BIR denied the protest, Asia United elevated the case to the CTA.

Asia United argues that since the FAN was issued on 31 January 2006 and the collection was only enforced on 18 December 2013, the five-year period of the BIR to collect has prescribed. The BIR argues that its right to collect has not yet prescribed considering Asia United's payment of the basic DST due and its repeated requests for the reduction, waiver, and abatement of the interest and increments.

Issue:

Has the BIR's right to collect the interest portion of the deficiency assessment prescribed?

Ruling:

Yes. The BIR's right to collect has prescribed. The FAN was received on 31 January 2006 hence, the BIR had until 31 January 2011 to collect the deficiency assessment.

Section 222 (c) and (d) of the Tax Code prescribes a period of five years following the assessment for the BIR to collect the tax by distraint or levy or proceeding in court, unless extended upon written agreement before expiration of the five year period.

The FAN has become final and executory as Asia United did not file a request for reinvestigation that could have suspended the running of the five year prescriptive period to collect. Asia United's acts of paying the principal deficiency DST and repeated requests for the reduction, waiver and abatement of interest would not justify the suspension of the prescriptive period for collection. The requests cannot be considered a request for reinvestigation that would toll the running of the five year collection period.

Thus, the Warrant of Distraint or Levy issued on 18 December 2013 may not be enforced by the BIR against Asia United for being barred by prescription.

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