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IN TAX | AUGUST 2008

CONGRESS

Republic Act (RA) No. 9505 or the Personal Equity and Retirement Account (PERA) Act of 2008 signed into law

The PERA ACT of 2008 was signed into law by President Arroyo last 22 August 2008. While the law takes effect 15 days following its publication in a newspaper of general circulation, the tax incentives that it grants shall take effect only on 01 January 2009.

The salient features of the PERA ACT of 2008 are as follows:

- Personal Equity and Retirement Accounts (PERA) is defined as the voluntary account established by and for the exclusive use and benefit of the contributor for purposes of being invested solely in PERA investment products in the Philippines. The PERA is to be administered by an entity ("administrator") accredited by the Bureau of Internal Revenue (BIR) and the funds placed in the custody of another entity ("custodian") accredited by the Bangko Sentral ng Pilipinas (BSP).
- A contributor, defined as any person with capacity to contract and has a tax identification number, is allowed to maintain not more than five PERA at any one time and to designate only one administrator for all his PERA. Every contributor is allowed to make a total maximum yearly contribution of P100,000.00 or its equivalent in foreign currency. If the contributor is married, each of the spouses will be entitled to make a contribution of P100,000.00. An OFW contributor, however, is allowed to make a contribution equal to double the maximum for a non-OFW contributor. A contributor is allowed to contribute more than the maximum contribution per year, however, the excess shall no longer be entitled to a tax audit of 5%. Refund of tax credits arising from the PERA contributions are not allowed,
- Employers can likewise contribute to their employees' PERA, which contributions will be allowed as deductions in the employer's gross income. The contributing employer must, however, comply with the mandatory SSS contributions and retirement pay under the Labor Code.
- All income earned from the investments and reinvestments of the maximum amount are tax exempt.

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- Distributions are allowed to be made upon reaching the age of 55 and the contributor has made contributions to the PERA for at least 5 years. All allowed distributions are likewise tax exempt. Any pre-termination or early withdrawal of the account shall be subject to early withdrawal penalties to be determined by the Secretary of Finance, subject to specified exemptions such as withdrawals for payments on account of total disability and hospitalization.
- The Department of Finance, Bureau of Internal Revenue (BIR), BSP, Securities and Exchange Commission (SEC), and the Insurance Commission were tasked to craft the implementing rules of the law.

SUPREME COURT

Third Division

Date-of-death valuation principle in determining net value of the estate

For estate tax purposes, the actual claims of creditors may be fully allowed as deductions from gross estate despite the fact that said claims were reduced or condoned through compromise agreements entered into by the estate with its creditors. There is no law, nor any legislative intent in the tax laws, which disregards the date-of-death valuation principle and particularly provides that post-death developments must be considered in determining the net value of the estate. Moreover, the term "claims" required to be presented against a decedent's estate is generally construed to mean debts or demands of a pecuniary nature which could have been enforced against the deceased in his lifetime, or liability contracted by the deceased before his death. Therefore, the claims existing at the time of death are significant to, and should be made the basis of the determination of allowable deductions. (*Rafael Arsenio S. Dizon vs. Court of Tax Appeals, et al., G.R. No. 140944, 06 May 2008*)

COURT OF APPEALS

Interest income on long-term fixed rate treasury notes

Interest income on long-term fixed rate treasury notes is not excluded from gross income under Section 32(B)(7)(g) of the Tax Code, as amended. While the term "gains" includes "interest" as a general rule, this rule cannot be applied to the cited provision of the Tax Code which particularly refers to gains realized from the sale or exchange or retirement of bonds, debentures and other certificate of indebtedness with a maturity of more than 5 years. Under the general definition of "gross income", there is a distinction between "gains derived from dealings in property" and "interests". Gains realized from the sale or exchange or retirement of bonds, debentures and other certificates of indebtedness would fall under the category "gains derived from dealings in property". On the other hand, interests would include interest from bonds, debentures and other certificate of



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If you have any comments, questions and suggestions you may contact us at 885-7000 loc. 339 or write us an email on manila@kpmg.com. We would be glad to hear from you.

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indebtedness. (*Malayan Reinsurance Corp. vs. CIR ,CA-G.R.. SP No. 74339, 24 April 2008*)

COURT OF TAX APPEALS (CTA)

En Banc

Tax exemption under “The Inventors and Inventions Incentives Act”

Under RA No. 7459, otherwise known as “The Inventors and Inventions Incentives Act”, any income derived from the sale of patented products is exempt from the payment of income taxes for a period of 10 years from the date of the product’s first sale on a commercial scale. The reason for this exemption is to encourage Filipino inventors to create more inventions and innovations beneficial to the people and to the country. To accept the view that the tax exemption commences only on the date of issuance of the BIR ruling approving the application for income tax exemption would not only be inconsistent with the express provision of RA No. 7459, but would also defeat the spirit and intent of the law. (*CIR vs. Splash Corporation, CTA EB No. 330, 05 May 2008*)

First Division

Imposition of business taxes under Sections 14 and 21 of the Manila Revenue Code constitutes double taxation

Subjecting a business entity to tax under both Sections 14 (tax on manufacturers) and 21 (a tax on businesses subject to excise, VAT or percentage taxes under the National Internal Revenue Code) of the MRC constitutes double taxation. Sections 14 and 21 of the MRC are based on Section 143 (a) and (h) of the Local Government Code (LGC) respectively. As such, the said MRC provisions should be interpreted in relation to Section 143 of the LGC, paragraph (a) of which imposes tax on manufacturers, assemblers, repackers, processors, brewers, distillers, rectifiers, and compounders of liquors, distilled spirits, and wines or manufacturers of any article of commerce of whatever kind or nature; while paragraph (h) thereof imposes tax “on any business, not otherwise specified in the preceding paragraphs, which the sanggunian may deem proper to tax: x x x.” The intent behind Section 143 in imposing business tax on a subject entity only once should likewise be applied in understanding and applying Sections 14 and 21 of the MRC. In other words, a subject entity held liable under Section 14 of the MRC, as amended, is debarred from being taxed under Section 21 of the same Code and vice versa. (*Unilever Philippines, Inc. vs. The Treasurer of the City of Manila, CTA Case No. 41, 24 June 2008*)

Second Division

Tax amnesty payment should be based on networth since there was failure to comply with the requirements to prove increase in networth



The Court ruled that since the taxpayer failed to comply with the requirements of the tax amnesty law, it cannot base the 5% tax amnesty rate on the alleged net increase of its networth; instead, the tax amnesty payment should have been based on the taxpayer's networth as of its June 2005 Statement of Assets, Liabilities and Networth (SALN). The taxpayer submitted the following to the Honorable Court: (1) DBP deposit slip showing tax amnesty payment; (2) Tax Amnesty Payment Form/Acceptance of Payment Form (BIR Form 0617), showing the computation of the tax amnesty payable in the amount of P500,000; (3) Notice of Availment of Tax Amnesty indicating with previous SALN/Balance Sheet; (4) SALN as of June 30, 2005, received on March 6, 2008; (5) SALN as of June 30, 2005 (Restated), also received by the BIR on March 6, 2008, and (6) Tax Amnesty Return (BIR Form 2116), showing the amnesty tax due of P500,000.

The tax amnesty payment of the taxpayer was computed based on the representation that it had previously filed a balance sheet/SALN, together with its income tax return for 2005. The taxpayer did **not** provide a copy of its 2005 income tax return. The Court ruled that the said requirements are necessary and that the taxpayer failed to establish the increase in its networth upon which the 5% tax amnesty rate was applied. Consequently, the Court ruled that the 5% tax amnesty payment should be computed on the taxpayer's networth. (*Tubuan Properties, Inc. vs. CIR, CTA Case No. 6570, April 21, 2008*)

BUREAU OF INTERNAL REVENUE

Update on draft IRR of RA 9504

The following is an exclusive update on the draft implementing rules and regulations of Republic Act No. (RA) 9504 entitled "An Act Amending Sections 22, 24, 34, 35, 51 and 79 of Republic Act No. 8424, As Amended, Otherwise Known as the National Internal Revenue Code of 1997" gathered during the 27 August 2008 forum at Makati Sports Club with Atty. Victoria G. Reinante, from the Office of the Deputy Commissioner-Operations Group of the BIR, as resource person.

Of interest are the following Transitory Provisions of the draft Revenue Regulations:

1. For the year 2008, the initial year of implementation of RA 9504, a transitory withholding tax table for the period from July 6 to December 31, 2008 has been recommended, determined by prorating the increased annual personal and additional exemptions under RA 9504 over the said period of six months. Thus, for individuals, regardless of personal status, the prorated personal exemption is P25,000.00, and P12,000.00 for each qualified dependent child (QDC) for the said period of 06 July to 31 December 2008.
2. Toward the end of 2008 and using the annualized withholding tax method, withholding agents are required to undertake the final year-end adjustments consolidating the compensation for the entire year of 2008 but taking into consideration the following transitory personal and additional exemptions

Personal Exemption	January 1 to July 5	July 6 to December 31	Total
Single	P10,000	P25,000	P35,000
Head of the family	12,500	25,000	37,500
Married	16,000	25,000	41,000
Additional Exemption for every QDC	4,000	12,500	16,500

Employers are required to ensure that tax due is equal to the tax withheld for the year-end adjustment computation. BIR Form No.1604-CF should be submitted on or before 31 January 2009.

3. For taxable year 2008, all employees already registered with the BIR must accomplish and file the Certificate of Update of Exemption and of Employer's and Employee's Information (BIR Form No. 2305), reflecting changes in information, if any. On the other hand, Application for Registration (BIR Form No.1902) will be used for employees with no TIN reflecting the claimed exemption. These forms shall be submitted together with the required documents/evidence of exemption.
4. The employers shall transmit both the original & duplicate copies of BIR Form No. 2305 (after accomplishing the portion of employer's information) with the RDO where the employee is registered.
5. Employees who fail to submit BIR Form No.2305/1902 with the required documents pursuant to the transition rules shall be classified under ZERO Exemption and shall be deemed to have waived the benefits of any exemption during the period until such time that the employee is able to submit the required forms and documents.
6. The alphabetical list of employees for 2008 shall be analyzed by the concerned BIR office by comparing the compensation figures reported in 2007 as against 2008 to ensure that there is no diminution in the compensation structure of employees.
7. Minimum wage earners whose compensation earned from January 1 to July 5, 2008 were not subjected to withholding tax but are, after considering the relevant exemptions, still subject to income tax, shall be required to file an income tax return covering the period from January 1 to July 5, on or before 15 April 2009.

Currently, the draft Revenue Regulations is being revised by the BIR based on the comments of the Department of Finance on the final draft implementing RA 9504.

Pre-audit for 2007 income and business tax returns of corporations and individuals

The BIR has authorized a pre-audit of 2007 income and business tax returns of corporations and individuals engaged in business and practice of profession with particular emphasis on the analysis of their tax compliance in relation to their gross sales/revenues/receipts. The pre-audit will be governed by the following guidelines:

- Taxpayers will be classified by industry or profession and then the ratio of their tax due against their gross sales/revenue/receipts will be determined. Based on the result of such analysis showing the normal or common ratio of income tax and business tax, a preliminary profile leading to industry/profession benchmark is established. Taxpayers with compliance below the normal or common benchmark within an industry/profession shall be selected for audit/verification.
- The computation of the ratio of tax compliance shall be as follows:

For Income Tax

$$\frac{\text{Tax Due Per Final Income Tax Return}}{\text{Gross Sales/Revenues/Receipts (whatever is applicable depending on the accounting method of the taxpayer)}}$$

For Business Tax

$$\frac{\text{Total Net VAT Payable for the Four Quarters (Line 25 of BIR Form No. 2550Q)}}{\text{Gross Taxable Sales/Revenues/Receipts (Whatever is applicable)}}$$

Or

$$\frac{\text{Total Percentage Tax Due for the Year (Line 19 of BIR Form No. 2551M or 2551Q)}}{\text{Total Taxable Amount/Base (Line 14C of BIR Form No. 2551Q)}}$$

- The pre-audit will also focus on the following:
 - a) Mathematical computation of the tax due and tax payment
 - b) Correctness of the application of Minimum Corporate Income Tax (MCIT), if applicable
 - c) Validity of claims for income tax holiday, tax exemption and other tax claimed incentives which resulted to non-payment or reduced payment of tax due
 - d) Correctness and validity of interest expense, contributions and representation expense
 - e) Completeness and accuracy of claimed creditable withholding taxes against tax due
 - f) Correct usage of tax credit certificates
 - g) Correct application of excess income tax carry-over or input tax carry-over; and
 - h) Correct application or offsetting of partial tax payments made before the due date of the tax

- Letters of Authority, Tax Verification Notices, Letter Notices and Mission Orders shall be issued to those whose tax compliance falls below the benchmark.

(Revenue Memorandum Order (RMO) No. 20-2008 dated 23 May 2008)

Guidelines released for short audit VAT returns for Q1 of 2008

The BIR has prescribed the guidelines for the short audit of the first quarter VAT returns for taxable year 2008 of taxpayers under the jurisdiction of the Large Taxpayers Service of the Regional offices. The audit/verification is based on the same selection criteria of RMO 20-2008.

(Revenue Memorandum Order (RMO) 22-2008 dated 5 June 2008)

Clarification of Issues Concerning Common Carriers by Air and Their Agents

Online international carriers cannot choose to be under the Value-added Tax (VAT) system and subject to VAT at zero-rate on their outbound international operations

Online international carriers cannot choose under the VAT system and subject to VAT at zero-rate on their outbound international operations similar to domestic air carriers registered as domestic corporations.

If the main business is exempt from VAT, the VAT-exempt person cannot elect that the said exempt business/es be placed under the VAT system. The option to be subject to VAT on its exempt transactions is available only to VAT-registered persons pursuant to Sec. 109(2) of the Code, as amended by RA 9337.

International airline company engaged in other activities subject to VAT cannot elect that all its business activities be subject to VAT.

The main or principal business of an international airline company is VAT-exempt because the same is subject to 3% percentage tax. Therefore, it cannot elect that its exempt principal business be subject to VAT even if its secondary businesses are subject to VAT.

The predominance test must be applied to determine the main or principal business of a taxpayer. If more than 50% of the taxpayer's gross sales and/or receipts come from business/es is subject to VAT, the taxpayer is a VAT person. Otherwise, the taxpayer cannot be a VAT person and thus, not eligible to elect that all exempt transactions be subject to VAT.

Domestic air carriers with international operations are subject to VAT at zero-rate and not to 3% percentage tax despite such international operations

The term "international air carrier" refers to foreign airline companies only. It does not include domestic airline corporations with international operation.

Income of domestic airline companies earned on cancelled tickets is subject to VAT.

All related income such as penalty or charges earned on the cancellation of tickets by the clients of domestic airline companies are subject to VAT.

(Revenue Memorandum Circular 46-2008 dated 21 February 2008)

Procedures in Handling Non-Large Taxpayers' Request for Transfer of Registration

In order to avoid disrupting the respective goals set for the Revenue Units of the BIR in accordance with the Attrition Act of 2005, the following rules are to be observed in case of a transfer by non-Large Taxpayers from one Revenue District Office (RDO) to another, :

- Transfers from one RDO to another shall be reflected in the BIR database at the end of the calendar year;
- Collections from the said taxpayer shall be credited not in the new RDO, but still in the old RDO, even if the said taxpayer has physically transferred its business address;
- The tax returns should be filed and payments made in any accredited agent bank located within the new RDO, but the taxpayer is mandated to use the old RDO code until the end of the calendar year. **This shall be an exception to the provision of Section 248 par A (2) of the Tax Code, as amended, regarding wrong venue in the filing of tax returns and payment of taxes;**
- The Transfer Confirmation Notice shall be issued by the new RDO to the old RDO at the end of the year for taxpayers who have filed the request for transfer; and
- All procedures enumerated under Revenue Memorandum Order (RMO) No.40-2004, as amended by RMO 11-2005 except as to those mentioned above shall be complied with.
(RMC 47-2008 dated 19 June 2008)

BUREAU OF CUSTOMS

Ecozones to be exempted from prohibition to import resins through warehouses

The ban on importations of resins (the raw material for plastic production under tariff headings 39.01 to 39.14) through Customs common bonded warehouses (CCBW) may soon be lifted for locators of economic zones. Last May, Customs Administrative Order (CAO) 4-2008 was issued banning the importation of resins through warehouses to curb smuggling. This resulted in the necessity for all companies to pay duties upfront on all importations of resins. The measure however was frowned upon by economic zone locators who depend on resins as a raw material requirement for their export products as it has required the said locators to go through the added administrative burden to file for duty drawback on each of their importations upon the exportation of their products. To remedy this, CAO 4-2008A was recently issued exempting economic zone locators who use resins as part of their raw materials for export production. *(CAO 4-2008 A dated 19 August 2008)*

New Collection District (No. XVI) created

Collection District No. XVI has been created by virtue of Executive Order 272. The Port of Limay in Bataan shall serve as the new District's principal port of entry and will have jurisdiction over the province of Bataan, except for the area under the Subic Bay Metropolitan Authority (SBMA). Its subport of entry will be Mariveles. Prior to the creation of the said Collection District, the Ports of Limay and Mariveles were under Collection District No. II-A (Port of Manila). Now under a separate administration, the new Collection District will have its own District Collector and Port Collector each assisted by one Deputy Collector. (See *CAO 5-2008 dated 03 July 2008*)

Two warehouse - system proposed

As measure to crackdown on smuggling, government is presently considering the possibility of shutting down all Customs Bonded Warehouses (CBWs) in the country except for two – a private one operated by the Philippine Exporters Confederation (Philexport), and a public one operated by the Philippine International Trading Corporation. Some 350 CBWs, intended to be temporary storage areas for raw materials entered duty free for eventual re-export, are currently in operation nationwide. The said warehouses have been regarded as conduits for smuggling on allegations that much of the products imported duty free under the scheme are diverted for domestic consumption, effectively avoiding the payment of proper duties and taxes. According to those proposing the 2 warehouse - system, maintaining only the 2 warehouses will facilitate the monitoring of imported raw materials. Various groups however, such as the Customs Bonded Warehouse Confederation, Inc. (CBWOC) oppose the said proposition.

Oil tariffs stay at 0%

Pursuant to the Certification issued by the Department of Energy dated 17 June and 21 July 2008 that the Cost Insurance Freight (CIF) price of Dubai crude and diesel in the international market have breached the levels of US\$103.50 per barrel and US\$117, respectively, tariffs on imported oil have remained at 0% for the months of July and August. (*Customs Memorandum Order 27 -2008 dated 20 June 2008 and CMO 30-2008 dated 25 July 2008*)

Duty exemptions on hybrid and CNG vehicles proposed

House Speaker Prospero Nograles and Agusan del Sur Representative Rodolfo Plaza have filed bills that, if approved, would exempt hybrid cars and vehicles that run on compressed natural gas (CNG) from customs duties. The introduction of the bill is part of an effort to reduce domestic demand for imported oil and lower carbon emissions by making fuel-efficient vehicles more affordable. The approval of this bill, according to the proponents, is expected to result in significant savings for both government and the people. Apart from granting tax exemptions, the proposal also instructs various Congressional Committees to prepare and deliberate on concrete proposals on how to develop hybrid and fuel optimizing technologies in the country



SECURITIES AND EXCHANGE COMMISSION

New deadline for filing of Annual Financial Statements

The deadline for the filing of Annual Financial Statements (“AFS”) for entities with financial accounting year ending on 31 December 2008 has been modified as follows:

1. In 2009, the deadline for the filing of the AFS will depend on the last digit of the SEC registration or license number of each entity, as follows:

<u>Filing Date</u>	<u>Last Digit</u>
April 20-24	1, 2, 3
April 27-30	4, 5
May 4-8	6, 7, 8
May 11-14	9, 0

2. The staggered filing dates apply to all corporations, including branch offices, representative offices, regional headquarters and regional operating headquarters of foreign corporations;
3. Before 20 April 2009, all corporations may file their AFS regardless of the last digit of their registration or license number;
4. Late filings will only be accepted starting May 15 and shall be subject to the prescribed penalties computed from the modified deadline applicable to the respective last digit of the SEC license stated in paragraph 1; and
5. Requests for extension of time to file the AFS or notifications of inability to file SEC Form 17-A under paragraph 1(F) of SRC Rule 17.1 will not be accepted.

(Securities and Exchange Commission Memorandum Circular No. 7 Series of 2008 dated 01 August 2008)