



2025

PURPLE NOTES



**ARELLANO UNIVERSITY SCHOOL OF LAW
BAR OPERATIONS COMMISSION**

TAXATION LAW

ARELLANO UNIVERSITY SCHOOL OF LAW BAR OPERATIONS COMMISSION 2025

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TABLE OF CONTENTS

TAXATION LAW

A. General Principles	4
1. Concept and Definition of Taxation	4
2. Inherent and Constitutional Limitations of Taxation	6
3. Requisites of a Valid Tax	22
4. Lifeblood Doctrine; Manifestations; Prohibition on Compensation and Set-off, Impact, Effect	22
5. Authority of Congress, Secretary of Finance, Commissioner of Internal Revenue (CIR)	23
6. Construction and Interpretation of Tax Laws, Rules, and Regulations	28
7. Double Taxation	29
a. Direct Duplicate Taxation	29
b. Indirect Duplicate Taxation	29
c. Mitigants	30
i. Tax Exemption	30
ii. Tax Credit	30
iii. Tax Deduction	31
iv. Tax Discount	31
v. Reciprocity Principle	31
8. Escape from Taxation	31
a. Shifting of Tax Burden	31
b. Tax Avoidance	32
c. Tax evasion	32
9. Tax Exemption	33
a. Nature – Exempt Person vs. Exempt Transaction	33
b. Express or Implied	33
c. Contractual	34
d. Construction of Tax Exemption Laws	34
e. Revocation	35
10. Compromise and Tax Amnesty	35
11. Taxpayer's Suit: Rationale and Requisites	35
B. National Internal Revenue Code of 1997 (NIRC), as amended by R.A. No. 10963, or the Tax Reform for Acceleration and Inclusion (TRAIN) Law Taxes and R.A. No. 11976 or the Ease of Paying Taxes Act	38
1. Income Tax	38
a. Nature and General Principles	38
i. Criteria in Imposing Philippine Income Tax	38
ii. Types of Philippine Income Taxes	38
iii. Kinds of Taxpayers – Individual, Corporations, Trusts, Estate	38
(a) Individual vs. Corporate Income Taxation – Schedular vs. Flat Rate	38
(b) Income Tax on Special Corporations	38
b. Income	51
i. Definition	51
ii. Realization and Recognition of Income	52
iii. Taxability of Income	53
iv. Income Sources	55

DO NOT REPRODUCE

ARELLANO UNIVERSITY SCHOOL OF LAW

BAR OPERATIONS COMMISSION 2025

(a) Compensation Income -----	55
(b) Professional Income -----	61
(c) Income from Business -----	61
(1) Active vs. Passive Income -----	61
(d) Income from Dealings in Property -----	65
(1) Capital vs. Ordinary Asset -----	65
(e) Situs of Income Taxation -----	67
(f) Gross Income vs. Net Income vs. Taxable Income -----	68
(1) Tax Deductions vs. Tax Credits -----	72
(2) Optional Standard Deduction -----	74
(g) Withholding Taxes -----	75
(1) Rationale -----	75
(2) Creditable vs. Withholding Taxes -----	76
(3) Duties of a Withholding Agent -----	77
2. Value-Added Tax (VAT) -----	78
a. Concept and Elements of VATable Transactions -----	78
b. Impact and Incidence of Tax -----	83
c. Destination Principle; Cross-Border Doctrine -----	84
d. Transactions Deemed Sale Subject to VAT -----	85
e. Zero-Rated Transactions -----	86
f. VAT Exempt Persons vs. VAT Exempt Transactions -----	89
g. Input and Output Tax -----	94
h. Tax Refund or Tax Credit -----	97
3. Tax Remedies -----	102
a. General Concepts -----	102
i. Tax Deficiency vs. Tax Delinquency -----	102
ii. Tax Evasion -----	102
b. Civil Penalties -----	103
i. Deficiency Interest and Delinquency Interest -----	103
ii. Surcharge -----	103
iii. Compromise Penalty -----	104
c. Assessment Process -----	105
i. Letter of Authority -----	106
ii. Submission of Supporting Documents by taxpayer -----	109
iii. Notice of Discrepancy -----	110
iv. Issuance of Preliminary Assessment Notice -----	111
v. Issuance of a Formal Letter of Demand/Final Assessment Notice -----	111
(a) Prescriptive Period for Assessment -----	116
(1) False Returns vs. Fraudulent Returns vs. Non-Filing Returns	
(b) Suspension of the Running of Statue of Limitations -----	122
d. Collection Process -----	122
i. Requisites -----	122
ii. Prescriptive Periods -----	123
e. Taxpayers Remedies -----	123
i. Protesting an Assessment -----	123
(a) Period to File Protest -----	124
(b) Effect of Failure to File Protest -----	124
ii. Submission of Supporting Documents by Taxpayer -----	125
iii. Decision of the Commissioner on the Protest -----	125
(a) Period to Act Upon or Decide on Protest Filed -----	125
(b) Remedies of the Taxpayer in case the CIR Denies the Protest	
or Fails to Act on the Protest -----	126

DO NOT REPRODUCE

ARELLANO UNIVERSITY SCHOOL OF LAW BAR OPERATIONS COMMISSION 2025

	(c) Effect of Failure to Appeal -----	126
iv.	Compromise and Abatement of Taxes -----	126
v.	Recovery of Tax Erroneously or Illegally Collected -----	128
	(a) Grounds, Requisites, and Period for Filing a Claim for Refund or Issuance of a Tax Credit Certificate -----	128
	(b) Proper Party to File Claim for Refund or Tax Credit -----	129
f.	Government Remedies -----	129
	i. Administrative Remedies -----	129
	(a) Tax Lien -----	129
	(b) Distrainment and Levy -----	129
	(c) Forfeiture of Real Property -----	130
	(d) Suspension of Business Operation -----	130
	ii. Judicial Remedies -----	130
	(a) Civil Action -----	130
	(b) Criminal Action -----	131
	(c) Non-Availability of Injunction on Collection -----	132

VIII. TAXATION LAW

A. GENERAL PRINCIPLES

1. CONCEPT AND DEFINITION OF TAXATION

Definition of Taxation

Taxation is the (1) power by which the sovereign, through its (2) law-making body, (3) raises revenue (4) to defray the necessary expenses of the government.

The process or means by which the sovereign, through its law-making body, raises income to defray the necessary expenses of government. It is a method of apportioning the cost of government among those who in some measure are privileged to enjoy its benefits and must, therefore, bear its burdens (*51 Am. Jur. 34; 1 Cooley 72-93*).

Taxation may be made the implement of the state's police power. (*Lutz vs. Araneta, GR No. L - 7859, December 22, 1955*)

Taxation is a destructive power which interferes with the personal and property rights of the people and takes from them a portion of their property for the support of the government. (*Paseo Realty and Development Corporation vs. CA, CTA and CIR, G.R. No. 119286, October 13, 2004*)

Definition of Tax

Taxes are enforced proportional contributions from persons and property, levied by the state by virtue of its sovereignty for the support of government and for the public needs. (*Colley, Taxation, 4th edition, p. 61, 1924*)

Taxes are the enforced proportional contributions exacted by the state from persons and properties pursuant to its sovereignty in order to support the government and to defray all the public needs. (*Mandanas vs. Purisima, G.R. No. 199802, July 03, 2018*)

Elements of Tax

- a. It is an enforced contribution. Payment of tax therefore is an obligation created by law. (*Dimaampao, Tax Principles and Remedies, p. 1-2, 2015 edition*)
- b. Its purpose is to raise revenues for public purposes. (*Ibid.*)
- c. It is proportional in character, since it is generally based on the one's property or ability to pay. (*Ibid.*)
- d. It is levied by authority of law. It cannot be exacted by the executive branch or by the Courts. The State's inherent power to tax is vested exclusively in the legislature. (*Id; Secretary of Finance Cesar B. Purisima vs. Representative Carmelo F. Lazartin, G.R. No. 210588, November 29, 2016*)

Characteristics of Taxation (CUPS)

a. Comprehensive

It applies to every trade or occupation, object of industry, use or enjoyment, and type of possession, imposing a burden that, if unpaid, may lead to seizure, sale, or confiscation of property. (*Churchill vs. Concepcion, G.R. No. 11572, September 22, 1916*)

b. Unlimited

It is unlimited in force and searching in extent that courts scarcely venture to declare that it is subject to any restrictions, except those that such rests into the discretion of the authority which exercises it. (*Ibid.*)

As a general rule, the power to tax is an incident of sovereignty and is unlimited in its range, acknowledging in its very nature no limits, so that security against its abuse is to be found only in the responsibility of the legislature which imposes the tax on the constituency who are to pay it (*Mactan Cebu International Airport Authority vs. Marcos, G.R. No. 120082, September 11, 1996*)

c. Plenary

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It is plenary in nature. Generally, the scope of the legislative power to tax is unlimited and plenary. (*Chamber of Real Estate and Builders' Associations, Inc. vs. Romulo, G.R. No. 160756, March 9, 2010*).

Operates on all persons and property belonging to the body politics; the original principle which has its foundation in society itself. It is granted by all for the benefit of all. (*Churchill vs. Concepcion, G.R. No. 11572, September 22, 1916*)

d. Supreme

No attribute of sovereignty is more pervading, and at no point does the power of the government affect more constantly and intimately all the relations of life than through exactions made under it. (*Ibid.*)

It is the strongest of all inherent powers of the government. (*Sison vs. Ancheta, G.R. No. L-59431, July 25, 1984*)

Theories and Basis of Taxation

a. Lifeblood Theory

Taxes are the lifeblood of the government. Without taxes, the government would be paralyzed and unable to operate. Hence, despite the natural reluctance to surrender part of one's hard-earned income, every person who is able must contribute his share in the running of the government. (*CIR vs. Algue, Inc., G.R. No. L-28896, February 17, 1988*)

b. Necessity Theory

The power to tax is an attribute of sovereignty. It is a power emanating from necessity. It is a necessary burden to preserve the State's sovereignty and a means to give the citizenry an army to resist an aggression, a navy to defend its shores from invasion, a corps of civil servants to serve, public improvements designed for the enjoyment of the citizenry and those which come within the State's territory, and facilities and protection which a government is supposed to provide. (*Phil. Guaranty Co., Inc. vs. CIR, G.R. No. L-22074, April 30, 1965*)

c. Symbiotic relationship theory or benefits protection theory

The basis of taxation is found in the reciprocal duties of protection and support between the state and its inhabitants. The state receives taxes that it may enable to carry its mandates into effect and perform the functions of government and the citizen pays the portion of taxes demanded in order that he may, by means thereof, be secured in the enjoyment of the benefits of an organized society. (*51 Am. Jur. 42-43*)

General Principles of Sound Tax System

a. Fiscal Adequacy

The sources of revenue should be sufficient to meet the demands of public expenditure in order to avoid fiscal deficit. (*Abakada Guro Party List vs. Ermita, G.R. Nos. 168056, 168207, 168461, 168463 & 168730, September 1, 2005*)

b. Theoretical Justice

The tax burden should be in proportion to the taxpayer's ability to pay. (*Ibid*)

c. Administrative Feasibility

The tax system should be capable of being effectively administered and enforced with the least inconvenience to the taxpayer. (*Municipality of Cainta vs. Pasig City, G.R. No. 176703 & 176721, June 28, 2017*)

Purpose of Taxation

a. Primary or Revenue Raising Purpose

The main purpose of taxation is for revenue collection in order for the State to operate, effect its functions, and for the welfare of its constituents (*Philippine Commission on Good Governance vs. Cojuangco, G.R. No. 147062-64, December 14, 2001*).

Fees may be properly regarded as taxes even though they also serve as an instrument of regulation. If the purpose is primarily revenue, or if revenue is, at least, one of the real and substantial purposes, then the exaction is properly called a tax (*Philippine Airlines, Inc. vs. Edu, G.R. No. L-41383, August 15, 1988*).

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b. Secondary or Non-revenue/Special /Regulatory Purpose

Taxation is no longer envisioned as a measure merely to raise revenue to support the existence of the government; taxes may be levied with a regulatory purpose to provide means for the rehabilitation and stabilization of a threatened industry which is affected with public interest as to be within the police power of the state. (*Caltex Philippines, Inc. vs. Commission on Audit, G.R. No. 92585 May 8, 1992*)

Taxation is also used for regulatory purposes or non-revenue objectives that may include:

i. Protection mechanisms for certain industries

The Supreme Court (SC) held that the Sugar Adjustment Act is an act enacted primarily under the police power and designed to obtain a readjustment of the benefits derived by people interested in the sugar industry as well as to rehabilitate and stabilize the industry which constitutes one of the great sources of the country's wealth and, therefore, affects a great portion of the population of the country. (*Lutz vs. Araneta, G.R. No. L-7859, December 22, 1955*)

ii. Regulation of activities under the guise of police power

The SC held that a tax provision which is imposition of 30% tax on gross receipts from rental or sale of videograms under Section 10 of Presidential Decree No. 1987 entitled "An Act Creating the Videogram Regulatory Board" is not a foreign to a regulatory law as it is simply one of the control mechanisms scattered therein. A tax does not cease to be valid merely because it regulates, discourages, or even definitely deters the activities taxed (*Tio vs. Videogram Regulatory Board, G.R. No. 75967, June 18, 1987*)

Taxation is a way of returning to the constituents of the State some expected economic or social benefit such as equitable distribution of wealth and income.

A tax serves a public purpose even if its legislative motive favors one group over another, as the State has the inherent power to choose the subjects of taxation. Any resulting inequities from taxing or exempting a specific class do not violate constitutional limits. (*Ferrer Jr vs. Bautista, G.R. No. 210551, June 30, 2015*)

2. INHERENT AND CONSTITUTIONAL LIMITATIONS OF TAXATION

a. INHERENT LIMITATIONS

The following are the inherent limitations of taxation:

1. **Public Purpose;**
2. **International Comity;**
3. **Non-Delegability of taxing power;**
4. **Exemption of Government Entities, Agencies, and Instrumentalities; and**
5. **Situs or Territoriality.** (*Ignatius Michael D. Ingles, Tax Made Less Taxing: A Reviewer with Codals and Cases, 3rd Edition, 2021, pp. 8-11*)

i. Public Purpose

A revenue measure must be laid for public purpose. It is the legislature who determines "public purpose". (*Dimaampao, Basic Approach to Income Taxation, 2018 Edition, p. 37*)

It is a general rule that the legislature is without power to appropriate public revenue for anything but a public purpose. It is the essential character of the direct object of expenditure which must determine its validity as justifying a tax, and not the magnitude of the interest to be affected nor the degree to which the general advantage of the community, and thus the public welfare, may be ultimately benefited by their promotion. Incidental to the public or to the state, which results from the promotion of private interest and the prosperity of private enterprises or

ARELLANO UNIVERSITY SCHOOL OF LAW BAR OPERATIONS COMMISSION 2025

business, does not justify their aid by the use of public money. (*Pascual vs. Secretary of Public Works and Communication*, G.R. No. L-10405, December 29, 1960)

Test in Determining Public Purpose in Tax

1. Duty Test – whether the thing to be threatened by the appropriation of public revenue is something which is the duty of the State, as a government.

The term "public purpose" is not defined. It is an elastic concept that can be hammered to fit modern standards.

Jurisprudence states that "public purpose" should be given a broad interpretation. It does not only pertain to those purposes which are traditionally viewed as essentially government functions, such as building roads and delivery of basic services, but also includes those purposes designed to promote social justice. Thus, public money may now be used for the relocation of illegal settlers, low-cost housing and urban agrarian reform. (*Planters Products, Inc. vs. Fertilizer Corporation*, G.R. NO. 166006, March 14, 2008)

2. Promotion of General Welfare Test – whether the law providing the tax directly promotes the welfare of the community in equal measure. When a tax law is only a mask to exact funds from the public when its true intent is to give undue benefit and advantage to a private enterprise, that law will not satisfy the requirement of "public purpose." (*Ibid.*)

The public purpose of a tax is not destroyed simply because it may disadvantage one group while benefiting another; such imbalance does not diminish the tax's public character. (*Tio vs. Videogram Regulatory Board*, G.R. No. 75697, June 19, 1987)

ii. International Comity

The Philippines adopts the generally accepted principles of international law as part of the law of the land and adheres to the policy of peace,

equality, justice, freedom, cooperation, and amity with all nations (*Section 2, Article II, 1987 Constitution*)

Comity means respect accorded by a State to other States due to being sovereign equals. Tax treaties are entered to minimize, if not eliminate the harshness of international juridical double taxation, which is why they are also known as double tax avoidance treaty or double tax avoidance agreement. [*Basic Taxation Law: Including the Ease of Paying Act (EOPT)*, p. 7-8, 2024 edition]

A state must recognize the generally accepted tenets of international law, among which are the principles of sovereign equality among the states and of their freedom from suit without their consent, that limit the authority of a government to effectively impose taxes on a sovereign state or instrumentalities, as well as on its property held, and activities undertaken, in that capacity. Even when one enters the territory of another, there is an implied understanding that the former does not thereby submit itself to the authority and jurisdiction of the latter. (*Mamalateo, Reviewer on Taxation*, 2019, pp. 56-57)

Treaty obligations must be performed in good faith, with local statutes and administrative issuances aligning appropriately. Administrative requirements, such as a prior application for treaty relief, should not supersede treaty benefits, especially in cases where a taxpayer seeks a refund due to non-availment of a tax treaty relief. (*Deutsche Bank AG vs. CIR*, G.R. No. 188550, August 19, 2013)

The Philippine Constitution provides for adherence to the general principles of international law as part of the law of the land. The time-honored international principle of pacta sunt servanda demands the performance in good faith of treaty obligations on the part of the states that enter into the agreement. In this jurisdiction, treaties have the force and effect of law (*CIR vs. Interpublic Group of Companies, Inc.*, G.R. No. 207039, August 14, 2019)

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The purpose of these international agreements is to reconcile the national fiscal legislations of the contracting parties in order to help the taxpayer avoid simultaneous taxation in two different jurisdictions. More precisely, the tax conventions are drafted with a view towards the elimination of international juridical double taxation, which is defined as the imposition of comparable taxes in two or more states on the same taxpayer in respect of the same subject matter and for identical periods. (*Ibid*)

Bearing in mind the rationale of tax treaties, the period of application for the availment of tax treaty relief as required by RMO No. 1-2000 should not operate to divest entitlement to the relief as it would constitute a violation of the duty required by good faith in complying with a tax treaty. The denial of the availment of tax relief for the failure of a taxpayer to apply within the prescribed period under the administrative issuance would impair the value of the tax treaty. At most, the application for a tax treaty relief from the BIR should merely operate to confirm the entitlement of the taxpayer to the relief. (*Ibid*)

iii. Non-Delegability of the Taxing Powers

General Rule: Congress could not re-delegate this delegated power, since the power of taxation is a power that is exercised by the Congress as delegates of the People.

In the legislature primarily lies the discretion to determine the nature (kind), object (purpose), extent (rate), coverage (subjects) and situs (place) of taxation. (*Chamber of Real Estate and Builders' Association, Inc. vs. Romulo, G.R. No. 160756, March 9 2010*)

Exceptions:

a. Delegation to Local Government Unit

The Constitution grants each LGU the power to create its own sources of revenue and to levy taxes, fees and charges which shall accrue exclusively to the LGU. (*Section 5, Article X, 1987 Constitution*)

Thus, interpreting statutory provisions on municipal fiscal powers, doubts will be resolved in favor of the municipal corporations. (*Quezon City et. al. vs. ABS-CBN Broadcasting Corporation, G.R. No. 162015, March 6, 2006*)

b. Delegation to the President

Delegation by Congress to the President to fix **tariff** rates, **import and export** quotas, **tonnage and wharfage** dues; and **other** duties or imposts. [*Section 28(2), Article VI, 1987 Constitution*]

Delegation to the President to enter into executive agreements, and to ratify treaties which may contain tax exemption provisions subject to the concurrence by the majority members of the Congress in the ratification made by the President. (*Section 28(4), Article VI, 1987 Constitution*)

c. Delegation to Specialized Administrative Agencies

The power to fill in the details and manner as to the enforcement and administration of a law may be delegated to various specialized administrative agencies like the Secretary of Finance in this case (*Taganito Mining Corp vs. CIR, G.R. No. 216656, April 26, 2021*)

Rules and regulations implementing the law are designed to fill in the details or to make explicit what is general, which otherwise cannot all be incorporated in the provision of the law. Such rules and regulations, when promulgated in pursuance of the procedure or authority conferred upon the administrative agency by law, "deserve to be given weight and respect by the courts in view of the rulemaking authority given to those who formulate them and their specific expertise in their respective fields." (*Ibid*)

To be valid, a revenue regulation must be within the scope of statutory authority or standard granted by the legislature. Specifically, the regulation must: (1) be germane to the object and purpose of the law; (2) not contradict, but conform to, the standards the law prescribes; and (3) be issued

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for the sole purpose of carrying into effect the general provisions of our tax laws. (*Ibid*)

iv. Exemption of Government Entities, Agencies, and Instrumentalities

Rationale: Taxes are financial burdens imposed for the purpose of raising revenues to defray the cost of the operation of the Government, and a tax on property of the Government, whether national or local, **would merely have the effect of taking money from one pocket to put it in another pocket.** (*Board of Assessment of Appeals of Laguna vs. CTA, G.R. No. L-35683, May 7, 1987*)

The practical effect of exemption is merely to reduce the amount of money that has to be handled by the government in the course of its operation (*Mactan Cebu International Airport Authority vs. Marcos, G.R. No. 120082, September 11, 1996*)

General Rule: Agencies performing governmental functions are tax-exempt.

Exceptions:

a. Agencies performing proprietary functions, unless expressly taxed.

b. Agencies performing government functions are subject to tax unless expressly taxed.

The government may choose to tax itself. Nothing prevents Congress from decreeing that even instrumentalities or agencies of the government performing government functions may be subject to tax. Where it is done precisely to fulfill a constitutional mandate and national policy, no one can doubt its wisdom. (*Ibid*)

c. Government-owned and controlled corporations (GOCCs) performing proprietary functions are subject to tax.

Exceptions to the exceptions:

a. Section 27(C) of the NIRC provides:

- i. Government Service Insurance System (GSIS)
 - ii. Social Security System (SSS)
 - iii. Philippine Health Insurance Corporation (PHIC)
 - iv. Local water districts
 - v. Home Development Mutual Fund (HDMF) or PAG-IBIG – exempt upon effectivity of CREATE Law
- b. Section 30 of the NIRC provides the following organizations shall not be taxed in respect to income received by them as such:
- i. Labor, agricultural or horticultural organization not organized principally for profit;
 - ii. Mutual savings bank not having a capital stock represented by shares, and cooperative bank without capital stock organized and operated for mutual purposes and without profit;
 - iii. A beneficiary society, order or association, operating for the exclusive benefit of the members such as a fraternal organization operating under the lodge system, or mutual aid association or a nonstock corporation organized by employees providing for the payment of life, sickness, accident, or other benefits exclusively to the members of such society, order, or association, or nonstock corporation or their dependents;
 - iv. Cemetery company owned and operated exclusively for the benefit of its members;
 - v. Nonstock corporation or association organized and operated exclusively for religious, charitable, scientific, athletic, or cultural purposes, or for the rehabilitation of veterans, no part of its net income or asset shall belong to or inure to the benefit of any member, organizer, officer or any specific person;
 - vi. Business league chamber of commerce, or board of trade, not organized for profit and no part of the net income of which inures to the benefit of any private stock-holder, or individual;

ARELLANO UNIVERSITY SCHOOL OF LAW BAR OPERATIONS COMMISSION 2025

- vii. Civic league or organization not organized for profit but operated exclusively for the promotion of social welfare;
- viii. A nonstock and nonprofit educational institution;
- ix. Government educational institution;
- x. Farmers' or other mutual typhoon or fire insurance company, mutual ditch or irrigation company, mutual or cooperative telephone company, or like organization of a purely local character, the income of which consists solely of assessments, dues, and fees collected from members for the sole purpose of meeting its expenses; and
- xi. Farmers', fruit growers', or like association organized and operated as a sales agent for the purpose of marketing the products of its members and turning back to them the proceeds of sales, less the necessary selling expenses on the basis of the quantity of produce finished by them;

Notwithstanding the provisions in the preceding paragraphs, 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.

v. Situs or Territoriality of Taxation

Section 42 (A) of the NIRC provides the guidelines in determining what income is sourced within the Philippines, whereas Section 42 (C) of the same law identifies what are income sourced without. The word "source" connotes "origin", the test is to determine if the income originated from the Philippines.

Situs of taxation literally means place of taxation. The power of tax may be exercised only within the jurisdiction of the taxing authority. [*Basic Taxation Law: Including the Ease of Paying Act (EOPT)*, p. 8, 2024 edition]

As a rule, the State's power to tax does not extend beyond its territorial limits. Case law holds that "[i]f an interest in property is taxed,

the situs of either the property or interest must be found within the State. If an income is taxed, the recipient thereof must have a domicile within the State or the property or business out of which the income issues must be situated within the State so that the income may be said to have a situs therein. Personal property may be separated from its owner and he may be taxed on its account at the place where the property is although it is not a citizen or resident of the State which imposes the tax." This territorial limitation of taxation is what necessitates the taxation of only income derived from sources "within" the Philippines for non-resident aliens and foreign corporations. (*Saint Wealth Ltd. vs. BIR*, G.R. Nos. 252965 & 254102, December 07, 2021)

The source of an income is the property, activity or service that produced the income. For the source of income to be considered as coming from the Philippines, it is sufficient that the income is derived from activity within the Philippines. In BOAC's case, the sale of tickets in the Philippines is the activity that produces the income. The tickets exchanged hands here and payments for fares were also made here in Philippine currency. The situs of the source of payments is the Philippines. The flow of wealth proceeded from, and occurred within, Philippine territory, enjoying the protection accorded by the Philippine government. In consideration of such protection, the flow of wealth should share the burden of supporting the government. (*CIR vs. British Overseas Airways Corp*, G.R. Nos. L-65773-74, April 30, 1987).

b. CONSTITUTIONAL LIMITATIONS

The following are examples of constitutional limitations to the power of taxation:

i. Due Process and Equal Protection

No person shall be deprived of life, liberty, or property without due process of law, nor shall any person be denied the equal protection of law. (*Section 1, Article III, 1987 Constitution*)

Due Process

Two kinds of due process:

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a. Substantive Due Process

An act is done under the authority of a valid law or Constitution itself

b. Procedural Due Process

An act is done after compliance with fair and reasonable methods or procedures prescribed by law.

Requirements of Due Process:

- a. Public Purpose
- b. Imposed within taxing authority's territorial jurisdiction
- c. Assessment or collection is not arbitrary or oppressive

The Commissioner exercises administrative adjudicatory power or quasi-judicial function in adjudicating the rights and liabilities of persons under the Tax Code. (*CIR vs. Avon Products Manufacturing, Inc., G.R. No. 201398-99, October 03, 2018*)

In carrying out these quasi-judicial functions, the Commissioner is required to "investigate facts or ascertain the existence of facts, hold hearings, weigh evidence, and draw conclusions from them as basis for their official action and exercise of discretion in a judicial nature." Tax investigation and assessment necessarily demand the observance of due process because they affect the proprietary rights of specific persons. (*Ibid*)

The due process clause may be invoked where a taxing statute is so arbitrary that it finds no support in the Constitution, as where it can be shown to amount to the confiscation of property. (*Sison, Jr. vs. Ancheta, G.R. L-59431, July 25, 1984*)

Instances of violations of the due process:

- a. If the tax amounts to confiscation of property;
- b. If the subject of confiscation is outside the jurisdiction of the taxing authority;
- c. If the tax is imposed for a purpose other than a public purpose;

d. If the law which is applied retroactively imposes just and oppressive taxes.

e. If the law violates the inherent limitations on taxation.

Equal Protection Clause

All persons subject to legislation shall be treated alike under similar circumstances and conditions both in the privileges conferred and liabilities imposed.

Equal protection clause applies only to persons or things identically situated and does not bar a reasonable classification of the subject of legislation. A classification is reasonable where:

1. Substantial distinctions which make real differences;
2. Germane to the purpose of the law;
3. Classification applies not only to present conditions but also to future conditions which are substantially identical to those of the present;
4. Classification applies only to those who belong to the same class. (*Ormoc Sugar Co., Inc. vs. Treasurer of Ormoc City, G.R. No. L-23794, February 17, 1968*)

ii. Non-Infringement of Religious Freedom

No law shall be made respecting an establishment of religion or prohibiting the free exercise thereof. The free exercise and enjoyment of religious profession and worship without discrimination or preference shall forever be allowed.^(SEP) No religious test shall be required for the exercise of civil or political rights. (*Section 5, Article III, 1987 Constitution*)

The free exercise clause is the basis of tax exemptions. The imposition of license fees on the distribution and sale of bibles and other religious literature by a non-stock, non-profit missionary organization not for purposes of profit amounts to a condition or permit for the exercise of their right, thus violating the constitutional guarantee of the free exercise and enjoyment of religious profession and worship which carries with it the right to disseminate religious beliefs and information.

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(American Bible Society vs. City of Manila, L-9637 April 30, 1957)

It is actually in the nature of a condition or permit for the exercise of the right. This is different from a tax in the income of one who engages in religious activities or a tax on property used or employed in connection with those activities. It is one thing to impose a tax on the income or property of a preacher. It is quite another thing to exact a tax for the privilege of delivering a sermon. (*Ibid*)

The Constitution, however, does not prohibit imposing a generally applicable tax on the sale of religious materials by a religious organization. (*Tolentino vs. Secretary of Finance, G.R. No. 115525, August 25, 1994*)

iii. Non-Infringement of Press Freedom

The 1987 Constitution guarantees that no law shall be passed abridging the freedom of speech, of expression, or of the press, or the right of the people peaceably to assemble and petition the Government for redress of grievances. (*Section 4, Article III, 1987 Constitution*)

As a general proposition, the press is not exempt from the taxing power of the State and that what the constitutional guarantee of free press prohibits are laws which single out the press or target a group belonging to the press for special treatment, or which in any way discriminate against the press on the basis of the content of the publication of R.A. No. 7716 (Expanded Value Added Law) is none of these. (*Ibid*)

Since the law granted the press a privilege, the law could take back the privilege anytime without offense to the Constitution. The reason was by granting exemptions, the State does not forever waive the exercise of its sovereign prerogative. (*Tolentino vs. Secretary of Finance, G.R. No. 115525, October 30, 1995*)

iv. Non-Impairment Clause

No law impairing the obligation of contracts shall be passed. (*Section 11, Article XII, 1987 Constitution*)

The Contract Clause has never been thought of as a limitation on the exercise of the State's power of taxation save only where a tax exemption has been granted for a valid consideration. (*Tolentino vs. Secretary of Finance, G.R. No. 115525, October 30, 1995*)

v. Prohibition Against Imprisonment for Non – Payment of Poll Tax

No person shall be imprisoned for debt or non-payment of a poll tax." (*Section 20, Article III, 1987 Constitution*)

Poll Tax, defined

A tax of fixed amount on individuals residing within a specified territory, whether citizens or not, without regard to their property. One cannot be imprisoned for non-payment of poll tax because payment thereof is not mandatory, it is merely permissive. (*51 Am. Jur. 660, cited in Villanueva vs. City of Iloilo, G.R. No. L-26521, December 28, 1968*)

While a person may not be imprisoned for non-payment of poll tax, he may be imprisoned for non-payment of other kinds of taxes where the law expressly so provides. (*Dimaampao, Tax Principles and Remedies, 2021 Edition, p. 118*)

Distinguish Tax from Debt	
Tax	Debt
Basis	
Law	Contract / Judgment
Effect of Failure to Pay	
Civil and criminal liability	Civil liability only
As to mode of payment	
Money	Money, property, or service
As to assignability	
No	Yes
As to subjectivity to compensation/ set-off	
No	Yes
As to interest	

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Yes, if deficient or delinquent	General rule: No, unless expressly stipulated
As to authority	
Public authority	Private individuals
Prescription	
Determined by the Tax Code	Determined by the Civil Code

vi. Appropriation, Revenue, Tariff Bill Must Exclusively Originate in the House of Representatives

All appropriation, revenue or tariff bills, bills authorizing the increase of public debts, bills of local application and private bills, shall originate exclusively in the House of Representatives, but the Senate may propose or concur with amendments. (*Sec. 24, Art. VI, 1987 Constitution*)

Indeed, what the Constitution simply means is that the initiative for filing revenue, tariff or tax bills, bills authorizing an increase of the public debt, private bills and bills of local application must come from the House of Representatives on the theory that, elected as they are from the districts, the members of the House can be expected to be more sensitive to the local needs and problems.

On the other hand, the senators, who are elected at large, are expected to approach the same problems from the national perspective. Both views are thereby made to bear on the enactment of such laws (*Abakada Guro Party List vs. Ermita, G.R. No. 168056, September 1, 2005*).

vii. Uniformity and Equitable Taxation

The rule of taxation shall be uniform and equitable. (*Section 28 par. 1, Article VI, 1987 Constitution*)

Uniformity in taxation means that all taxable articles or kinds of property of the same class shall be taxed at the same rate. Different articles may be taxed at different amounts provided that the rate is uniform on the same class everywhere with all people at all times.

(*British American Tobacco vs. Camacho, G.R. No. 163583, April 15, 2009*)

A tax is uniform when it operates with the same force and effect in every place where the subject of it is found. (*CIR vs. Lingayen Gulf Electric Power Co., G.R. No. L-023771, August 4, 1988*)

Different articles or other subjects may be taxed at different rates provided that the rate is uniform on the same class everywhere. (*City of Baguio vs. De Leon, G. R. No. L-24756, October 31, 1969*)

A local tax on tenement houses does not violate the rule of uniformity and equality of taxation even if the tax in question is not also levied on other classes of buildings in the locality where such tax is imposed. (*Villanueva vs. City of Iloilo, G.R. No. L-26521, December 28, 1968*)

Uniformity is not disregarded if a tax is levied on admission to cinema, theaters, vaudeville companies, theatrical shows and boxing exhibitions but does not tax other places of amusement such as race tracks, cockpits, cabarets, concert halls, circuses and other places of amusement. (*Eastern Theatrical Co. vs. Alfonso, G.R. No. L-1104, May 31, 1949*)

It must be stressed that the **rule of uniform taxation does not deprive Congress of the power to classify subjects of taxation**, and only demands uniformity within the particular class. (*Abakada Guro Party List vs. Ermita, G.R. No. 168056, September 1, 2005*)

Uniformity vs. Equitability vs. Equality

Uniformity – All taxable property shall be alike to be subjected to tax.

Equitability – The burden of taxation falls to those better able to pay.

Equality – When the burden of the tax falls equally and impartially upon all persons and property subject to it.

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The law is also equitable even if it is equipped with a threshold margin. The VAT rate of 0% or 10% (now 12%) does not apply to sales of goods or services with gross annual sales or receipts not exceeding P1,500,000.00 (now P3,000,000). Also, basic marine and agricultural food products in their original state are still not subject to tax, thus ensuring that prices at the grassroots level will remain accessible (*Abakada Guro Party List vs. Ermita, G.R. No. 168056, September 1, 2005*)

viii. Progressive System of Taxation

The Congress shall evolve a progressive system of taxation. (*Section 28 (1), Article VI, 1987 Constitution*)

Progressivity — A tax system is progressive when it is designed to reduce income inequality by increasing the tax burden as the taxable income increases. [*Basic Taxation Law: Including the Ease of Paying Act (EOPT), p. 9, 2024 edition*]

Progressivity of taxation is also mandated by the Constitution. Our income tax system is one good example of such progressivity because it is built on the principle of the taxpayer's ability to pay. Taxation is progressive when its rate goes up depending on the resources of the person affected (*Reyes vs. Almanzor, G.R. Nos. 49839-46, April 26, 1991*).

Non-Prohibition of Regressive tax

The Constitution does not really prohibit the imposition of indirect taxes which, like the VAT, are regressive. **What it simply provides is that Congress shall "evolve a progressive system of taxation."** The constitutional provision has been interpreted to mean simply that "direct taxes are to be preferred [and] as much as possible, indirect taxes should be minimized." (*Tolentino vs. Secretary of Finance, GR No. 115455, October 30, 1995; Abakada Guro Partylist vs. Ermita GR No. 168056, September 1, 2005*)

ix. Grant by Congress of Authority to the President to Impose Tariff Rates

The Congress may, by law, authorize the President to fix within specified limits and subject to such limitations and restrictions as it may impose, tariff rates, import and export quotas, tonnage and wharfage dues, and other duties or imports within the framework of the national development program of the government. (*Section 28 (2), Article VI, 1987 Constitution*)

Flexible Tariff Clause

Requisites of a valid imposition of tariff rates by the President:

1. **Delegated** by Congress through a law;
2. Subject to **Congressional limits** and restrictions; and
3. Within the **framework** of the national development program (*Section 28 (2), Article VI, 1987 Constitution*)

x. Exemption of Properties Used for Religious and Charitable Entities (*Section 28 (3), Article VI, 1987 Constitution*)

Charitable institutions, churches and parsonages or convents appurtenant thereto, mosques, non-profit cemeteries, and all lands, buildings and improvements, actually, directly and exclusively used for religious, charitable, or educational purposes shall be exempt from taxation." (*Section 28 (3), Article VI of the 1987 Constitution*)

In order to be entitled to the constitutional exemption from REAL PROPERTY TAX, it must be clear and unequivocal proof that (i) it is a charitable institution; and (ii) its real properties are **ACTUALLY, DIRECTLY and EXCLUSIVELY** used for charitable purposes. (*Lung Center of the Phil. vs. Quezon City, G.R. No. 144104, June 29, 2004*)

"Exclusive" is defined as possessed and enjoyed to the exclusion of others; debarred from participation or enjoyment; and **"exclusively"** is defined, in a manner to exclude; as enjoying a privilege exclusively. If

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real property is used for one or more commercial purposes, it is not exclusively used for the exempted purposes but is subject to taxation. The words "dominant use" or "principal use" cannot be substituted for the words "used exclusively" without doing violence to the Constitution and the law. (*Id.*)

What is meant by actual, direct and exclusive use of the property for charitable purposes is the direct and immediate and actual application of the property itself to the purposes for which the charitable institution is organized. It is not the use of the income from the real property that is determinative of whether the property is used for tax-exempt purposes. (*Id.*)

Actual use is necessary. To be exempt from tax, the lands, buildings and improvements must not only be exclusively but also actually and directly used for religious and charitable purposes. (*Province of Abra vs. Hernando, G.R. No. L-49336, August 31, 1981*)

USE overrides OWNERSHIP that if property, although actually owned by a religious, charitable or educational institution, is actually used for a non-exempt purpose, the exemption from tax of said property vanishes. (*Abra Valley vs. Aquino, G.R. No. L-39086, June 15, 1988*)

While the use of the second floor of the main building for residential purposes of the Director and his family may find justification under the concept of incidental use, which is complementary to the main or primary purpose, i.e., educational, the lease of the first floor to the Northern Marketing Corporation cannot be considered incidental to the purpose of education. Since only a portion is used for the purpose of commerce, it is only fair that half of the assessed tax be returned to the school involved. (*Id.*)

The exemption in favor of property used exclusively for charitable or educational purposes is not limited to property actually indispensable therefor but extends to facilities which are incidental to and reasonably necessary for the accomplishment of said

purposes, such as in the case of hospitals, a school for training nurses, a nurses home, property use to provide housing facilities for interns, resident doctors, superintendents, and other members of the hospital staff and recreational facilities for student nurses, interns, and residents' such as athletic fields. (*Id.*)

Rule on Gifts in Favor of Charitable and other Institutions

General Rule: The constitutional exemption applies only to property tax. Gifts are subject to donor's tax. (*Rev. Casimiro Lladoc vs. CIR, G.R. No. L-19201, June 16, 1965*)

Exemption: Gifts made in favor of charitable and other institutions may also be exempt from Donor's tax, not under the Constitution, but under the NIRC, provided certain conditions are met. (*Sections 101(A)(2) & 101(B)(2), NIRC as amended by TRAIN Law*)

xi. Prohibition Against Taxation of Educational Institutions

a. Non-Stock, Non-Profit Educational Institution

All revenues and assets of non-stock, non-profit educational institutions used **actually, directly and exclusively** used for educational purposes shall be exempt from taxes and duties. (*Section 4 par. 3 sub-par. 1, Article XIV, 1987 Constitution*)

Requisites for availing the tax exemption under Article XIV, Section 4 (3), are as follows: (1) the taxpayer falls under the classification "non-stock, non-profit educational institution"; and (2) the income it seeks to be exempted from taxation is used actually, directly and exclusively for educational purposes. (*CIR vs. Young Men's Christian Association of the Philippines, G.R. No. 124043, October 14, 1998*)

b. Proprietary Educational Institutions

Proprietary educational institutions, including those cooperatively owned, may likewise be

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entitled to such exemptions subject to the limitations provided by law, including restrictions on dividends and provisions for reinvestment (*Section 4 par. 3 sub-par. 2, Article XIV, 1987 Constitution*)

Subject to conditions prescribed by law, all grants, endowments, donations, or contributions used actually, directly, and exclusively for educational purposes shall be exempt from tax. (*Section 4 par. 2, Article XIV, 1987 Constitution*)

Entitlement to tax exemption under this provision involves two tests:

1. Revenue or asset sought to be taxed used **MUST be actually, directly, and exclusively for educational purposes; AND**
2. Entity seeking exemption **MUST be a non-stock, non-profit educational institution.**

Differentiation between the tax exemption of non-stock non-profit (NSNP) educational institution and proprietary educational institution

NSNP	Propriety
As to requisites	
Conditioned only on to the actual, direct, and exclusive use of their revenue and assets for educational purposes	Subject to the limitations imposed by Congress.
As to treatment under the Tax Code	
Tax-exempt entity under Section 30 (Exemption from Tax on Corporation) of the Tax Code	Covered by Section 27 (Rates of Income tax on Domestic Corporation) of the Tax Code

A proprietary educational institution is entitled only to the reduced rate of 10% corporate

income tax if: (1) the proprietary educational institution is non-profit; and (2) its gross income from unrelated trade, business or activity does not exceed 50% of its total gross income. (*Section 27(B), NIRC 1997, as amended by R.A. Nos. 10963 [TRAIN], 11256, 11346, 11467 and 11534 [CREATE]*)

A nonstock and nonprofit educational institution and government educational institution shall not be taxed in respect to income received by them. [*Section 30(H) & 30(I), NIRC 1997, as amended by R.A. Nos. 10963 (TRAIN), 11256, 11346, 11467 and 11534 (CREATE)*]

Notwithstanding the provisions in the Section 30, 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. (*last par. of Section 30, NIRC 1997, as amended by R.A. Nos. 10963 [TRAIN], 11256, 11346, 11467 and 11534 [CREATE]*)

A plain reading of the Constitution would show that Article XIV, Section 4(3) does not require that the revenues and income must have also been sourced from educational activities or activities related to the purposes of an educational institution. The phrase all revenues is unqualified by any reference to the source of revenues.

So long as the revenues and income are used actually, directly and exclusively for educational purposes, then said revenues and income shall be exempt from taxes and duties.

Thus, when a non-stock, non-profit educational institution proves that it uses its revenues actually, directly, and exclusively for educational purposes, it shall be exempted from income tax, value-added tax, and local business tax. (*CIR vs. DLSU, G.R. No. 196596, 198841 & 198941, November 9, 2016*)

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The privilege granted to non-stock non-profit educational institutions is conditioned only on the actual, direct and exclusive use of their revenues and assets for educational purposes and cannot be subject to limitations imposed by law. (*Id.*)

Thus, the last paragraph of Section 30 of the Tax Code which 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" is without force and effect for being contrary to the Constitution insofar as it subjects to tax the income and revenues of non-stock, non-profit educational institutions used actually, directly and exclusively for educational purpose. (*Id.*)

Exemption from Real Property Tax

Charitable institutions, churches and personages or convents appurtenant thereto, mosques, non-profit cemeteries, and all lands, buildings, and improvements, **actually, directly, and exclusively used for** religious, charitable, or **educational purposes** shall be exempt from taxation. (*Section 28 (3), Article VI, 1987 Constitution*)

When a non-stock, non-profit also shows that it uses its assets in the form of real property for educational purposes, it shall be exempted from real property tax. (*CIR vs. DLSU, G.R. No. 196596, 198841 & 198941, November 9, 2016*)

Summary of Application of Non-Stock, Non-Profit Educational Institutions

Income Tax, VAT and Local Business Tax	Real Property
As to determination	
Revenues were used ADE for educational purposes, and NOT the source of income	Property or asset was used ADE for educational purposes

xii. Exemption Majority Vote of Congress for Grant of Tax Exemption (Section 28 par. 4, Article VI, 1987 Constitution)

No law granting any tax exemption shall be passed without the concurrence of a majority of all the Members of the Congress." (*Section 28 (4), Article VI, 1987 Constitution*)

Reason: To prevent indiscriminate grant of tax exemptions.

In granting tax exemptions, an absolute majority of the members of the Congress is required, while in cases of withdrawal of such tax exemption, a relative minority is sufficient. (*Dimaampao, Tax Principles and Remedies, 2021 ed.*)

An exemption granted by a presidential proclamation and not by law is therefore invalid. (*John Hay People's Alternative Coalition vs. Lim, G.R. No. 119775, October 24, 2003*)

xiii. Prohibition on Use of Tax Levied for Special Purpose

All money collected or any tax levied for special purposes shall be treated as a special fund and paid out for such purpose only. If the purpose for which a special fund was created has been fulfilled or abandoned, the balance, if any, shall be transferred to the general funds of the government. (*Section 29 par. 3, Article VI of the 1987 Constitution*)

xiv. President's Veto Power on Appropriation, Revenue or Tariff Bills

The President shall have the power to veto any particular item or items in an **appropriation, revenue or tariff bill** but the veto shall not affect the item or items which he does not object. (*Section 27 (2), Article VI, 1987 Constitution*)

xv. Non-Impairment of Supreme Court's Jurisdiction

The Congress shall have the power to define, prescribe, and apportion the jurisdiction of the various courts but may not deprive the Supreme Court of its jurisdiction over cases

ARELLANO UNIVERSITY SCHOOL OF LAW BAR OPERATIONS COMMISSION 2025

enumerated in Section 5 hereof. (*Section 5(2)(b), Article VIII, 1987 Constitution*)

The Supreme Court shall have, among others, the following powers:

1. Review, revise, reverse, modify, or affirm on appeal or certiorari, as the law or the Rules of Court may provide, final judgments and orders of lower courts;
2. All cases involving the legality of any tax, impost, assessment, or toll, or any penalty imposed in relation thereto. (*Section 5, Article VIII, 1987 Constitution*)

Under the **Principle of Judicial Non – Interference:**

The courts cannot inquire into the wisdom of the taxing act unless there is a violation of the Constitutional limitations or restrictions. (*CIR vs. Lingayen Gulf Electric Power Co., Inc. GR L 237771, August 4, 1968*)

The Constitution, as a fundamental law, overrides any legislative or executive act that runs counter to it. Where it can be demonstrated that the challenged statutory provisions fail to abide by its command, then the courts must so declare and adjudged it null. (*ABAKADA GURO vs. Ermita, G.R. No. L-24756, October 31, 1968*)

xvi. Grant of Power to the Local Government Units to Create its Own Sources of Revenue

Each local government unit shall have the power to create its own sources of revenues and to levy taxes, fees and charges subject to such guidelines and limitations as the Congress may provide, consistent with the basic policy of local autonomy. Such taxes, fees, and charges shall accrue exclusively to the local governments.” (*Section 5, Article X, 1987 Constitution*)

By necessary implication, the legislative power to create political corporations for purposes of local self-government carries with it the power to confer on such local governmental agencies the power to tax. (*Pepsi-Cola Bottling Corp. of*

the Phil. vs. City of Butuan, G.R. No. L-22814, August 28, 1968)

When local governments invoke the power to tax on national government instrumentalities, the exercise of the power is construed strictly against local governments. The rule is that a tax is never presumed and there must be a clear language in the law imposing the tax. (*MIAA vs. CA, G.R. No. 155650, July 20, 2006*)

Although the power to tax is inherent in the State, the same is not true for the LGUs to whom the power must be exercised within the guidelines and limitations that Congress may provide. Provinces, cities, municipalities and barangays are not the sovereign; rather, they are mere "territorial and political subdivisions of the Republic of the Philippines."

Therefore, the power of a province to tax is limited to the extent that such power is delegated to it either by the Constitution or by statute. (*City of Manila vs. Colet, G.R. Nos. 120051, 121613, 121675, 121704, 121720-28, 121847-55, 122333, 122335, 122349 & 124855, December 10, 2014*)

xvii. No Appropriation or Use of Public Money for Religious Purposes

No public money or property shall be appropriated applied, paid or employed, directly or indirectly, for the use, benefit or support of any sect, church, denomination, sectarian institution or system of religion, or of any priest, preacher, minister, other religious teacher, or dignitary as such, except when such priest, preacher, minister, or dignitary is assigned to the armed forces, or to any penal institution, or government orphanage or leprosarium. (*Section 29[2], Article VI, 1987 Constitution*)

xviii. Right to Privacy

The right of the people to be secure in their persons, houses, papers, and effects against unreasonable searches and seizures of whatever nature and for any purpose shall be inviolable. (*Section 2, Article III, 1987 Constitution*)

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The privacy of communication and correspondence shall be inviolable except upon lawful order of the court, or when public safety or order requires otherwise, as prescribed by law. (*Section 3, Article III, 1987 Constitution*)

The right to privacy or the right to be left alone, in Philippine jurisdiction, is accorded recognition independent from the right to liberty and deserves full constitutional protection. As such, regulations that are alleged to be violative of the right to privacy must be subject to strict scrutiny which requires that the State must show that the regulation not only serves a compelling interest but is also narrowly drawn in order to prevent abuses. (*Philippine Stock Exchange vs. Secretary of Finance, G.R. No. 213860, July 5, 2022*)

The government agencies have failed to show that the means to be employed under the regulations are the least restrictive for effecting the invoked interest. The investors are not assured that the information they will provide will be protected and will not be used for any other purpose. (*Id.*)

The collection of information mandated by the regulations was not necessary for the BIR to perform its functions. The BIR did not even allege any problems encountered in the collection of taxes that would require the need for more specific disclosure as sought by the regulations. While the BIR showed that it was mandated to collect personal information pursuant to its revenue mandate, the specific regulations failed the test of necessity. (*Id.*)

The mandatory registration of appointment books under Section 2(2) of RR No. 4-2014 is an unconstitutional intrusion into the fundamental rights of professionals and their patients and clients. It violates privacy rights and the ethical norms of the professionals. (*IBP vs. Secretary of Finance, G.R. No. 211772, April 18, 2023*)

The appointment books of professionals, such as lawyers, doctors, accountants, or dentists, contain their clients' names and the date and time of consultation, information over which they reasonably expect privacy. Mandating the registration of appointment books to monitor tax compliance would be an unreasonable State intrusion into their right to privacy. It was pointed out that Section 2(1) of RR No. 4-2014 is valid only insofar as it mandates self-employed individuals, as proper subjects of taxation, to register and pay annual registration fees. Section 2(2), which obligates the registration of books of accounts, is likewise valid as it simply implements the Tax Code. (*Id.*)

Difference between the power of taxation of national government and local government units

National Government	Local Government
As to source of taxing power	
Inherent	Delegated by Congress through the 1987 Constitution (<i>Art. X, Sec. 5</i>) and Local Government Code of 1991
As to scope of taxing power	
Has plenary and comprehensive taxing power, subject only to constitutional limitations	The power is limited, both substantively and procedurally
As to legislative authority	
National Internal Revenue Code (NIRC)	Local tax ordinances enacted by the Sangguniang Panlungsod, Bayan, or Panlalawigan pursuant to the LGC

(*City of Manila vs. Colet, G.R. No. 120051, December 10, 2014*)

ARELLANO UNIVERSITY SCHOOL OF LAW BAR OPERATIONS COMMISSION 2025

3. REQUISITES OF A VALID TAX

Requirements for a tax law to be valid:

- It must be for a **public purpose**;
- It must be **uniform**;
- The party being taxed must be **within the jurisdiction** of the taxing authority;
- The tax must not impugn on the inherent and constitutional **limitations** on the power of taxation; and
- Assessment and collection of certain kinds of taxes guarantee against injustice to individuals, especially by providing **notice and opportunity for hearing**.

4. LIFEblood DOCTRINE; MANIFESTATIONS; PROHIBITION ON COMPENSATION AND SET-OFF, IMPACT, EFFECT

Lifeblood theory

Taxation is the indispensable and inevitable price for civilized society; without taxes, the government would be paralyzed for lack of motive power to activate and operate it. Thus, the collection of taxes must be made without hindrance if the State is to maintain its orderly existence

However, such collection should be made in accordance with law as any arbitrariness will negate the very reason for government itself. It is therefore necessary to reconcile the apparently conflicting interests of the authorities and the taxpayers so that the real purpose of taxation, which is the promotion of the common good, may be achieved (*Commissioner of Internal Revenue vs. Algue*, G.R. No. L- 28896, February 17, 1988).

Prohibition On Compensation and Set-Off

General Rule:

There can be no off-setting of taxes against the claims that the taxpayer may have against the government. A person cannot refuse to pay a tax on the ground that the government owes him an amount equal to or greater than the tax

being collected. (*Francia vs. Intermediate Appellate Court*, G.R. No. L-67649, June 28, 1988 citing *In. Re: Cordero vs. Gonda*, G.R. No. L-22369, October 15, 1966)

The law on compensation is not applicable when the parties are not mutual creditors and debtors. A claim for taxes is not such a debt, demand, contract or judgment as is allowed to be set-off under the statutes of set-off.

The general rule, based on grounds of public policy, is well-settled that no set-off is admissible against demands for taxes levied for general or local governmental purposes (*Republic vs. Mambulao Lumber Co.*, G.R. No. L-17725, Feb 28, 1962)

Taxes are not subject to set-off or compensation for the following reasons:

- Taxes are of distinct kind, essence and nature, and these impositions cannot be classed in merely the same category as ordinary obligations;
- The applicable laws and principles governing each are peculiar, not necessarily common, to each other; and
- Public policy is better subserved if the integrity and independence of taxes are maintained. (*Id.*)

Reasons:

- Lifeblood Doctrine;
- Taxes are not contractual obligation but arise out of duty to the government;
- The government and the taxpayer are not mutually creditors and debtors of each other. (*Francia vs. IAC*, G.R. No. L-67649, June 28, 1988)

A person cannot refuse to pay tax on the basis that the government owes him an amount equal to or greater than the tax being collected. The collection of a tax cannot await the results of a lawsuit against the government. (*Philex Mining Corp. vs. CIR*, G.R. No. 125704, 1998; *Francia vs. Intermediate Appellate Court*, G.R. No. L-67649, 1988)

Exceptions:

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Where both claims already became overdue and demandable as well as fully liquidated, or where the government and the taxpayer are in their own right reciprocally debtors and creditors of each other, compensation takes place by operation of law. (*Domingo vs. Garlitos*, G.R. No. L-18994, June 29, 1963)

In several cases, as an exception to offsetting, the Court has allowed the determination of the taxpayer's liability in a refund case, thereby allowing the offsetting taxes. In these cases, offsetting was allowed because the determination of the taxpayer's liability is intertwined with the resolution for the claim of refund.

- Thus, a tax presently being assessed against a taxpayer **may not** be recouped or set-off against an overpaid tax the refund of which is already barred by prescription (*Domondon*, 11th ed, p. 46)
- A tax is not an obligation that is created by contracts express or implied. It is an obligation imposed by law. Inasmuch as taxes are not debt, it follows that the two obligations are not subject of set-off or compensation under Art. 1279 of the New Civil Code. (*Domingo vs. Garlitos*, G.R. No. L-18994, June 29, 1963)
- Taxes could not be set-off against the taxpayer's claim of refund for reforestation charges it initially shouldered which should have been the obligation of the government. (*Republic vs. Mambulao Lumber*, G.R. No. L-17725, February 28, 1962)
- The obligation to pay real estate tax delinquency could not be set-off by the amount which the government is indebted to the former by way of expropriation that was effected by the national government. (*Francia vs. IAC*, G.R. No. L-67649, June 28, 1988)
- There can be no offsetting of taxes against the claims that a taxpayer may have against the government, such as reimbursement from the Oil Price Stabilization Fund (OPSF). (*Caltex Phils. vs. COA*, G.R. No. 92585, May 8, 1992)

- Philex cannot refuse the payment of its tax liabilities on the ground that it has pending claims for VAT input credit/refund. A taxpayer cannot refuse to pay his taxes when they fall due simply because he has a claim against the government or that the collection of the tax is contingent on the result of the lawsuit it filed against the government. (*Philex Mining vs. Commissioner*, G.R. No. 125704, August 28, 1998)
- In the case of TPC, where it filed a claim for refund or credit under Sec. 112 of the NIRC while the issue to be resolved is whether TPC is entitled of its unutilized input VAT, the offsetting was not allowed. The Court held that, since it is not a claim for refund under Section 229 of the NIRC, the correctness of TPC's VAT returns is not an issue. Hence, the determination of the taxpayer's liability was not related with the resolution of the claim for refund or credit offsetting was also not an issue. (*CIR vs. Toledo Power Company*, G.R. No. 196415, 2015)

5. AUTHORITY OF CONGRESS, SECRETARY OF FINANCE, COMMISSIONER OF INTERNAL REVENUE

a. Authority of the Congress

The power of taxation, being an essential and inherent attribute of sovereignty, belongs, as a matter of right, to every independent government, and needs no express conferment by the people before it can be exercised. It is purely legislative and, thus, cannot be delegated to the executive and judicial branches of government without running afoul to the theory of separation of powers. (*Film Development Council of the Philippines vs. Colon Heritage Realty Corporation*, G.R. No. 203754, June 16, 2015)

b. Authority of the Secretary of Finance

Upon recommendation of the CIR, the Secretary of Finance shall promulgate all

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needful rules and regulations for the effective enforcement of the provisions of the NIRC. (*Sec. 244, NIRC*)

Powers and Duties of the BIR

- i. The **assessment and collection** of all internal revenue taxes, fees, and charges;
- ii. The **enforcement** of all forfeitures, penalties, and fines connected therewith;
- iii. The **execution of judgments** in all cases in its favor by the CTA and ordinary courts;
- iv. **Giving effect to and administering** the supervisory and police powers conferred to it by the Tax Code or other laws. (*Sec. 2, NIRC*)

c. Authority of the CIR

i. Power to Interpret Tax Laws

The power to interpret the provisions of the NIRC and other tax laws shall be under the exclusive and original jurisdiction of the Commissioner, subject to review by the Secretary of Finance. (*Sec. 4, NIRC*)

NOTE: A ruling by the CIR that interprets provisions of the NIRC and other tax laws shall be presumed valid unless modified, reversed or superseded by the Secretary of Finance. A taxpayer who receives an adverse ruling from the CIR may, within thirty (30) days from the date of receipt of such ruling, seek its review by the Secretary of Finance. The Secretary of Finance may also review the rulings *motu proprio*. (*DOF Order 7-02*)

ii. Power to Decide Tax Cases

The CIR shall have the power to decide the following tax cases but subject to the exclusive appellate jurisdiction of the CTA:

- a. **Disputed assessments**,
- b. **Refunds** of internal revenue taxes, fees or other charges,
- c. The **penalties** imposed in relation thereto, or
- d. **Other matters** arising under the Tax Code, other tax laws or portions thereof administered by the BIR. (*Sec. 4, NIRC*)

In any case, even if this Court were to disregard the Collection Letter as a final decision of the Commissioner on Avon's protest, the Collection Letter constitutes an act of the Commissioner on "other matters" arising under the NIRC which, pursuant to *Philippine Journalists, Inc. vs. CIR*, may be the subject of an appropriate appeal before the Court of Tax Appeals. (*CIR vs. Avon Products Manufacturing, G.R. Nos. 201398-99, October 03, 2018*)

iii. Power to obtain information, and to Summon, Examine, and Take Testimony of Person

The CIR has the power to obtain information for the purpose of ascertaining the correctness or existence of a tax return, determining the tax liability, collecting taxes or in evaluating tax compliance. The CIR may:

- a. To **examine** any book, paper, record, or other data which may be relevant or material to such inquiry;
- b. To **obtain** on a regular basis from any person other than the person whose internal revenue tax liability is subject to audit or investigation, or from any office or officer of the national and local governments, government agencies and instrumentalities, including the Bangko Sentral ng Pilipinas and government-owned or -controlled corporations, any information such as, but not limited to, costs and volume of production, receipts or sales and gross incomes of taxpayers, and the names, addresses, and financial statements of corporations, mutual fund companies, insurance companies, regional operating headquarters of multinational companies, joint accounts, associations, joint ventures of consortia and registered partnerships, and their members;

Provided, That the Cooperative Development Authority shall submit to the Bureau a tax incentive report, which shall include information on the income tax, value-added tax, and other tax incentives availed of by

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ARELLANO UNIVERSITY SCHOOL OF LAW BAR OPERATIONS COMMISSION 2025

cooperatives registered and enjoying incentives under Republic Act No. 6938, as amended: Provided, further, That the information submitted by the Cooperative Development Authority to the Bureau shall be submitted to the Department of Finance and shall be included in the database created under Republic Act No. 10708, otherwise known as 'The Tax Incentives Management and Transparency Act (TIMTA)'

c. To **summon** the person liable for tax or required to file a return, or any officer or employee of such person, or any person having possession, custody, or care of the books of accounts and other accounting records containing entries relating to the business of the person liable for tax, or any other person, to appear before the Commissioner or his duly authorized representative at a time and place specified in the summons and to produce such books, papers, records, or other data, and to give testimony;

d. To take such **testimony** of the person concerned, under oath, as may be relevant or material to such inquiry; and

e. To cause revenue officers and employees to make a **canvass** from time to time of any revenue district or region and inquire after and concerning all persons therein who may be liable to pay any internal revenue tax, and all persons owning or having the care, management or possession of any object with respect to which a tax is imposed.

The provisions of the foregoing paragraphs notwithstanding, nothing in this Section shall be construed as granting the Commissioner the authority to inquire into bank deposits other than as provided for in Section 6(F) of the NIRC. (*Sec. 5, NIRC*)

It is the power to hear and determine questions of fact to which the legislative policy is to apply and to decide in accordance with the standards laid down by the law itself in enforcing and administering the same law. The administrative body exercises its quasi-judicial power when it

performs in a judicial manner an act which is essentially of an executive or administrative nature, where the power to act in such manner is incidental to or reasonably necessary for the performance of the executive or administrative duty entrusted to it (*CIR vs. Avon Products Manufacturing, G.R. Nos. 201398-99, October 03, 2018*).

In carrying out these quasi-judicial functions, the Commissioner is required to "investigate facts or ascertain the existence of facts, hold hearings, weigh evidence, and draw conclusions from them as basis for their official action and exercise of discretion in a judicial nature." Tax investigation and assessment necessarily demand the observance of due process because they affect the proprietary rights of specific persons. (*Id.*)

With respect to the BIR, its Commissioner is authorized to examine books, paper, record, or other data of taxpayers but only to ascertain the correctness of any return, or in making a return when none was made, or in determining the liability of any person for any internal revenue tax, or in collecting such liability, or evaluating the person's tax compliance. The BOC, on the other hand, is authorized to audit or examine all books, records, and documents of importers necessary or relevant for the purpose of collecting the proper duties and taxes. Since there are no taxes or duties involved in this case, the BIR and the BOC likewise have no power and authority to open and examine the books of accounts. (*Commission on Audit vs. Pampilo Jr., G.R. Nos. 188760, 189060 & 189333, June 30, 2020*)

iv. Power to Inquire into Bank Deposit Accounts and Other Related information held by Financial Institutions

The CIR has the power to inquire into bank deposits and other related information held by financial institutions of the following:

a. A decedent, to determine his gross estate;

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b. A taxpayer who filed an application for compromise of tax liability by reason of financial incapacity. Such taxpayer must waive his bank secrecy privilege in writing, and such waiver shall constitute the authority of the CIR to make the inquiry;

c. A taxpayer subject of a request of a foreign tax authority, for the supply of information pursuant to an international convention or agreement. The information obtained in this may be used by the BIR for assessment, audit, and enforcement. The exchange of information with the foreign tax authority must be done in a secure manner to ensure confidentiality.

The foreign tax authority must provide the following:

- i. Identity of the taxpayer under examination;
- ii. Information sought, its nature and form;
- iii. Purpose;
- iv. Grounds for believing that the information is within Philippine jurisdiction;
- v. Name and address of the person believed to be in possession of the requested information;
- vi. A statement that the request is in conformity with the law of the foreign tax authority;
- vii. A statement that the requesting foreign authority has exhausted all means available in its own territory except those that would give rise to disproportionate difficulties. (Sec. 6(F), NIRC)

vi. Power to Examine returns and Determine the tax due

Examine returns and determine the tax due. After a return has been filed, the CIR or his duly authorized representative may authorize the examination of a taxpayer and the assessment of the correct tax, notwithstanding any law requiring prior authorization of any government agency or instrumentality. Failure

to file a return shall not prevent the CIR from authorizing the examination of a taxpayer. (Sec. 6(A), NIRC)

Best Evidence Obtainable Doctrine

The CIR shall assess the proper tax based on the best evidence obtainable when the report required by law as the basis for the assessment was not submitted, or when there is reason to believe that such report is false. (Sec. 6(B), NIRC)

Tax returns cannot be withdrawn once filed but may be amended within three years from the date of filing, unless a notice of audit or investigation. (Id.)

The law is specific and clear. The rule on the "best evidence obtainable" applies when a tax report required by law for the purpose of assessment is not available or when the tax report is incomplete or fraudulent (*Bonifacio Sy Po vs. CA, G.R. NO. 81446, August 18, 1988*)

vii. Power to Conduct Inventory-taking, Surveillance and to Prescribe Presumptive Gross Sales and Receipts

The CIR may, at any time during the taxable year, order inventory-taking of goods of any taxpayer as a basis for determining his internal revenue tax liabilities, or may place the business operations of any person, natural or juridical, under observation surveillance if there is reason to believe that such person is not declaring his correct income, sales or receipts for internal revenue tax purposes. (Sec 6(C), NIRC)

The findings may be used as the basis for assessing the taxes for the other months or quarters of the same or different taxable years and such assessment shall be deemed prima facie correct.

BIR Commissioner Caesar Dulay in 2018 thru a Tax Advisory dated January 31, 2018 made use of this section when he obligated the taxpayer to pay monthly withholding taxes rather than quarter as per TRAIn Law.

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vii. Power to Terminate Taxable Period

The CIR shall declare the tax period of a taxpayer terminated at any time, and shall request immediate payment of the tax for such period, if it came to the CIR's knowledge that:

- a. The taxpayer is retiring from business subject to tax;
- b. The taxpayer is intending to leave the Philippines or conceal his property; or
- c. The taxpayer is performing any act tending to obstruct the proceedings for the collection of the tax for the past or current quarter or year, or to render the same totally or partly ineffective, unless such proceedings are begun immediately. (*Sec. 6(D), NIRC*)

viii. Power to Prescribe Real Property Values

The CIR is authorized to divide the Philippines into different zones for the purpose of determining the fair market value of real properties in each zone. This is known as the zonal value.

The following are the process of prescribing the zonal valuation:

1. **Mandatory consultation** with both private and public competent appraisers before division of the Philippines into zones.
2. Prior **Notice** to affected taxpayers before the determination of fair market values of the real properties.
3. **Publication** or posting of adjustments in zonal value in newspaper of general circulation in the province, city or municipality concerned.
4. The basis of valuation and records of consultation shall be **public records** open to the inquiry of the taxpayer.
5. **Zonal valuations** shall be automatically adjusted every three years.

For purposes of computing any internal revenue tax, the value of the property shall be, whichever is the higher of:

- a. The fair market value as determined by the Commissioner; or
- b. The fair market value as shown in the schedule of values of the Provincial and City Assessors.

ix. Power to prescribe procedure and documentary requirements

The CIR may prescribe the manner of compliance with procedural and additional documentary requirements in connection with the preparation or submission of financial statements accompanying tax returns.

x. Power to Delegate

The Commissioner may delegate the powers vested in him under the pertinent provisions of this Code to any or such subordinate officials with the rank equivalent to a **division chief or higher**, subject to such limitations and restrictions as may be imposed under rules and regulations to be promulgated by the Secretary of Finance, upon recommendation of the Commissioner.

However, the following powers of the Commissioner **shall not be delegated**:

- a. Power to recommend the promulgation of **rules and regulations**;
- b. Power to **issue rulings of first impression**;
- c. Power to reverse, revoke or modify any existing ruling of the BIR;
- d. Power to **compromise or abate**, under Sec. 204 of the Tax Code, any tax liability, except the following which may be compromised by the Regional Evaluation Board:
 - i. Assessments issued by the regional offices involving basic deficiency taxes of Five hundred thousand pesos (P500,000) or less; and
 - ii. minor criminal violations

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ARELLANO UNIVERSITY SCHOOL OF LAW BAR OPERATIONS COMMISSION 2025

- e. Power to **assign or reassign** internal revenue officers to establishments where articles subject to excise tax are produced or kept. (*Sec. 7, NIRC*)

xi. Power of the Commissioner to Suspend the Business Operations of a Taxpayer

The Commissioner or his authorized representative is hereby empowered to suspend the business operations and temporarily close the business establishment of any person for any of the following violations:

- a. In the case of a VAT-registered person:

- i. Failure to issue receipts or invoices;
- ii. Failure to file a value-added tax return as required under Section 114; or
- iii. Understatement of taxable sales or receipts by thirty percent (30%) or more of his correct taxable sales or receipts for the taxable quarter.

- b. Failure of any Person to Register as Required under Section 236.

The temporary closure of the establishment shall be for the duration of not less than five (5) days and shall be lifted only upon compliance with whatever requirements prescribed by the Commissioner in the closure order. (*Sec. 115, NIRC*)

6. CONSTRUCTION AND INTERPRETATION OF TAX LAWS, RULES AND REGULATIONS

Construction and Interpretation of Tax Law

Statutes levying taxes or duties are to be construed strongly against the Government and in favor of the subject or citizens, because burdens are not to be imposed or presumed to be imposed beyond what statutes expressly and clearly declare. No person or property is subject to taxation unless they fall within the

terms or plain import of a taxing statute. (*CIR vs. CA, G.R. No. 86785, November 21, 1991*)

Laws granting tax deductions, refunds, exemption are construed in *strictissimi juris* against the taxpayers and liberally in favor of the taxing authority. **Any claim for tax exemption from tax statutes is strictly construed against the taxpayer and it is contingent upon the taxpayer to establish a clear right to tax exemption.** Tax exemptions are strictly construed against the grantee and liberally in favor of the taxing authority. They are looked upon with disfavor. They are held strictly against the taxpayer and if not expressly mentioned in the law, must at least be within its purview by clear legislative intent. (*CIR vs. Arnoldus Carpentry Shop, Inc., G.R. No. 71122, March 25, 1988*)

This rule also applied to tax amnesties which are never favored nor presumed in law. (*CIR vs. Transfield Philippines, Inc., G.R. No. 211449, January 16, 2019*)

When Congress grants an exemption to a national government instrumentality from local taxation, such exemption is construed liberally in favor of the national government instrumentality. The reason for the general rule does not apply in the case of exemptions running to the benefit of the government itself or its agencies. The practical effect of an exemption is merely to reduce the amount of money that must be handled by the government in the course of its operations. (*MIAA vs. CA, G.R. No. 155650, July 20, 2006*)

Requisites of a valid revenue regulation

For tax rules and regulations to be valid:

- i. Must be germane to the object and purpose of the law;
- ii. Must not contradict, but conform to, the standards the law prescribes; and
- iii. Must be issued for the sole purpose of carrying into effect the general provisions of our tax laws. (*La Suerte Cigarette Factory vs. CIR, G.R. No. 125346, November 11, 2014*)

ARELLANO UNIVERSITY SCHOOL OF LAW BAR OPERATIONS COMMISSION 2025

Non-Retroactivity of Rulings

Any revocation, modification or reversal of (1) rules and regulations promulgated in accordance with the NIRC, or (2) any rulings or circulars promulgated by the CIR shall not be given retroactive application if the revocation, modification, or reversal is prejudicial to the taxpayers. (*Sec. 246, NIRC*)

Exceptions:

- i. Where the taxpayer deliberately misstates or omits material facts from his return or any document required of him by the BIR;
- ii. Where the facts subsequently gathered by the BIR are materially different from the facts on which the ruling is based; or
- iii. Where the taxpayer acted in bad faith.

Good faith cannot be invoked on the basis of previous BIR issuances if the same were not issued in its favor. (*San Miguel Corp. vs. Commissioner of Internal Revenue, G.R. Nos. 257697 & 259446, April 12, 2023*)

However, when the ruling, circular, or rules and regulations was nullified by a court (and not by the CIR), then the non-retroactivity rule does not apply. (*Philippine Bank of Communications vs. CIR, G.R. No. 112024, 1999*)

A general interpretative rule issued by the CIR may be relied upon by taxpayers from the time the rule is issued up to its reversal by the Commissioner or this Court. (*CIR vs. San Roque, G.R. No. 187485, 2013*)

The rules and regulations that administrative agencies promulgate, which are the product of a delegated legislative power to create new and additional legal provisions that have the effect of law, should be within the scope of the statutory authority granted by the legislature to the administrative agency. It may not make rules and regulations which are inconsistent with the provisions of the Constitution or a statute, particularly the statute it is administering or which created it, or which are in derogation of, or defeat, the purpose of a statute. **In case of conflict between a statute and an administrative order, the**

former must prevail. (*Soliman vs. Santos, G.R. Nos. 202417 & 203245, July 25, 2023*)

7. DOUBLE TAXATION

Kinds of taxation

1. Direct double taxation
2. Indirect double taxation

a. DIRECT DUPLICATE TAXATION OR DOUBLE TAXATION IN STRICT SENSE

There is direct duplicate taxation when the same taxpayer is taxed twice for the same purpose by the same taxing authority within the same jurisdiction during the same taxing period, and the taxes are of the same kind or character. (*Nursery Care Corp. vs. Acevedo, G.R. No. 180651, July 30, 2014*)

Same property is taxed twice when it should be taxed only once; and that both taxes are imposed on the same property or subject matter for the same purpose, by the same State, Government or taxing authority within the same jurisdiction or taxing district during the same taxing period and covering the same kind of character of tax. It violates the equal protection clause of the constitution. (*Villanueva vs. City of Iloilo, G.R. No. L-26521, December 28, 1968*)

Requisites of Direct Duplicate Taxation:

1. Both taxes are imposed on the same property or **subject matter**;
2. For the same **purpose**;
3. Imposed by the same **taxing authority**;
4. Within the same **jurisdiction**;
5. During the same **taxing period**;
6. Covering the same **kind or character** of tax. (*City of Manila vs. Coca-Cola Bottlers Philippines, Inc., G.R. No. 181845, August 4, 2009*)

b. INDIRECT DUPLICATE TAXATION OR DOUBLE TAXATION IN BROAD SENSE

Opposite of direct duplicate taxation and is not legally objectionable. The absence of one or more of the foregoing requisites of obnoxious

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direct tax makes it indirect. (*Mamalateo, Reviewer on Taxation, 2019, p. 25*)

Constitutionality of Double Taxation

There is no constitutional prohibition against double taxation in the Philippines. It is something not favored, but is permissible, provided some other constitutional requirement is not thereby violated. (*Villanueva vs. City of Iloilo, G.R. No. L-26521, December 28, 1968*)

Double taxation becomes obnoxious only when the taxpayer is taxed twice for the benefit of the same governmental entity or by the same jurisdiction for the same purpose, but not in a case where one tax is imposed by the State and the other by the city or municipality. (*Pepsi Cola vs. Tanauan, G.R. No. L-31156, February 27, 1976*)

Double taxation in its stricter sense is unconstitutional, but that in the broader sense is not necessarily so. (*Mamalateo, Reviewer on Taxation, 2019, p. 25*)

General Rule: Our Constitution does not prohibit double taxation, in a broad sense. Hence, it may not be invoked as a defense against the validity of tax laws. (*Ibid.*)

DIRECT DOUBLE TAXATION (Prohibited)	INDIRECT DOUBLE TAXATION (Allowed)
<ol style="list-style-type: none"> Both taxes are imposed on the same property or subject matter; For the same purpose; Imposed by the same taxing authority; Within the same jurisdiction; During the same taxing period; 	<p>Extends to all cases in which there are two or more pecuniary impositions but one or more of the requisites of direct double taxation is missing. (i.e. VAT and LBT imposed on same revenue)</p>

6. Covering the same kind or character of tax.	
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(*Villanueva vs. City of Iloilo, G.R. No. L-26521, December 28, 1968*)

Exception: Double taxation will not be allowed if it results in a violation of the equal protection clause.

There is no double taxation in the following instances:

- Tax imposed by the State and the local government upon the same occupation, calling or activity. (*Villanueva vs. City of Iloilo, G.R. No. L-26521 December 28, 1968*)
- Real estate tax and income tax collected on the same real property leased for earning purposes. (*Ibid.*)
- Taxes are imposed on the taxpayer's final product and the storage of raw materials used in the production of the final product. (*Procter and Gamble Philippines vs. Municipality of Jagna, G.R. No. L-24265, December 8, 1979*)

c. MITIGANTS

i. Tax Exemption

Exemption is an immunity or privilege; it is freedom from a charge or burden to which others are subjected. (*Greenfield vs. Meer, G.R. No. 156, September 27, 1946*)

The essence of tax exemption is the immunity or freedom from a charge or burden to which others are subjected. It is a waiver of the government's right to collect what would have been otherwise collectible. (*Secretary of Finance vs. Lazatin, G.R. No. 210588, November 29, 2016*)

ii. Tax Credit

It generally refers to an amount that is "subtracted directly from one's total tax liability." It is an "allowance against the tax itself" or "a deduction from what is owed" by a

ARELLANO UNIVERSITY SCHOOL OF LAW BAR OPERATIONS COMMISSION 2025

taxpayer to the government. (*CIR vs. Central Luzon Drug Corporation, G.R. No. 159647, April 15, 2005*)

iii. Tax Deduction

This is defined as a subtraction from income for tax purposes, or an amount that is allowed by law to reduce income prior to the application of the tax rate to compute the amount of tax which is due. (*CIR vs. Central Luzon Drug Corporation, G.R. No. 159647, April 15, 2005*)

Tax Credit	Tax Deduction
Reduces the tax due that is determined after applying the corresponding tax rates to taxable income	Reduces the income that is subject to tax in order to arrive at taxable income
Used AFTER the tax has been computed	Used BEFORE the tax has been computed

(*CIR vs. Central Luzon Drug Corporation, G.R. No. 159647, April 15, 2005*)

iv. Tax Discount

A tax discount typically refers to a reduction or decrease in the amount of taxes payable by a taxpayer, as provided by law or administrative regulation.

In the Philippines, tax discounts are often provided in local taxation under the Local Government Code (LGC) of 1991 (Republic Act No. 7160). Section 251 of the LGC authorizes local government units (LGUs) to grant tax discounts for advance prompt payment of real property tax.

v. Reciprocity Principle

The reciprocity principle in taxation law involves a number of bilateral treaties which the Philippines has entered into for the avoidance of double taxation. The purpose of these international agreements is to reconcile the national fiscal legislations of the contracting parties in order to help the taxpayer avoid simultaneous taxation in two different jurisdictions. More precisely, the tax

conventions are drafted with a view towards the elimination of international juridical double taxation. (*CIR vs. SC Johnsons & Sons, Inc., G.R. No. 127105, June 25, 1999*)

To eliminate double taxation, a tax treaty resorts to two methods: first, by allocating the right to tax between the contracting states; and second, where the state of source is assigned the right to tax, by requiring the state of residence to grant a tax relief either through exemption or tax credit. (*Cargill Philippines, Inc. vs. Commissioner of Internal Revenue, G.R. No. 203346, September 9, 2020*)

The exemption and credit principles are the two leading principles in eliminating double taxation that are being followed in existing conventions between countries.

Under the exemption principle, the income that may be taxed in the state of source is not taxed in the state of residence. This may be applied by two methods: full exemption, where the state of residence does not account for the income from the state of source for tax purposes; or with progression, where the income taxed in the state of source is not taxed by the state of residence, but the state of residence retains the right to consider that income when determining the tax to be imposed on the rest of the income.

Under the credit principle, the state of residence retains the right to tax the taxpayer's total income, but allows a deduction for the tax paid in the state of source. It may be applied by two methods: a full credit, where the total amount of tax paid in the state of source is allowed as deduction; or an ordinary credit, where the deduction allowed by the state of residence is restricted to that part of its own tax appropriate to the income from the state of source. (*Id.*)

8. ESCAPE FROM TAXATION

a. SHIFTING OF TAX BURDEN

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The burden of tax payment is transferred from the statutory taxpayer to another without violating the law (e.g., VAT).

It must be emphasized that only indirect taxes could be shifted. (*Maibarara Geothermal, Inc. vs. Commissioner of Internal Revenue* (G.R. No. 250479, July 18, 2022))

When the seller passes on the tax to his buyer, he, in effect, shifts the tax burden, not the liability to pay it, to the purchaser as part of the price of goods sold or services rendered. To put the situation in graphic terms, by taking the VAT due to the selling price, the seller remains the person primarily and legally liable for the payment of the tax. What is shifted only to the intermediate buyer and ultimately to the final purchaser is the burden of the tax. Stated differently, a seller who is directly and legally liable for payment of an indirect tax, such as the VAT on goods or services, is not necessarily the person who ultimately bears the burden of the same tax. It is the final purchaser or end-user of such goods or services who, although not directly and legally liable for the payment thereof, ultimately bears the burden of the tax. (*Pepsi-Cola Bottling Co. of the Philippines, Inc. vs. Municipality of Tanauan*, G.R. No. L-31156, February 27, 1976)

Impact of Taxation	Incidence of Taxation
The point on which a tax is originally imposed	the point on which a tax burden finally rest or settle down

(*CIR vs. COMELEC*, G.R. No. 244155, May 11, 2021)

b. TAX AVOIDANCE

Tax avoidance and tax evasion are the common devices wherein the taxpayer can escape the effects of taxation. (*Ignatius Michael D. Ingles, Tax Made Less Taxing: A Reviewer with Codals and Cases, 3rd Edition, 2021, p.23*).

Tax avoidance, though reducing tax obligations, remains lawful as long as it

adheres to legislative intent and does not circumvent established tax obligations through deceit. (*Commissioner of Internal Revenue vs. YMCA*, G.R. No. 124043, October 14, 1998)

It is the use by the taxpayer of legally permissible alternative tax rates or methods of assessing taxable property or income in order to avoid or reduce tax liability (e.g. termination of deposits subject to 20% final tax and re-investing it in tax-exempt government bonds). It is a saving device within the means sanctioned by law and should be used by the taxpayer in good faith and at arm's length. (*CIR vs. Estate of Benigno Toda*, GR 147188, September 14, 2004).

c. TAX EVASION

It is the use of taxpayers of illegal or fraudulent means to evade or lessen the payment of a tax (e.g. deliberate non-reporting or under-reporting of an income). (*Id.*)

Indicia of Fraud in Tax Evasion

Failure to declare for taxation purposes true and actual income derived from business for 2 consecutive years; or

Substantial under-declaration of revenues in the income tax returns of the taxpayer for 4 consecutive years coupled with intentional overstatement of deductions. (*see Sec. 248(B), NIRC*)

Connotes the integration of three (3) factors:

- The end to be achieved, i.e., the payment of less than that known by the taxpayer to be legally due;
- An accompanying state of mind which is described as being "evil", in "bad faith", "willful", or "deliberate and not merely accidental", and
- A course of action or failure of action which is unlawful. (*CIR vs. Estate of Benigno Toda*, GR 147188, September 14, 2004)

NOTE: See also Section 248(B) of NIRC providing for prima facie evidence of filing a false or fraudulent return.

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Tax Avoidance	Tax Evasion
The tax saving device within the means sanctioned by law. This method should be used by the taxpayer in good faith and at arm's length.	A scheme used outside of those lawful means and when availed of, it usually subjects the taxpayer to further or additional civil or criminal liabilities. Tax evasion connotes
Legal	Illegal

9. TAX EXEMPTION

i. Nature – Exempt Person vs. Exempt Transaction

No law granting any tax exemption should be passed without the concurrence of a **majority** of all the members of Congress (*Section 28(4), Article VI, 1987 Constitution*).

Basic Principles Regarding Tax Exemption

- Exemptions are highly disfavored by law and he who claims an exemption must be able to justify his claim by the clearest grant of law. An exemption from the common burden cannot be permitted to exist upon vague implication. (*Asiatic Petroleum Co. vs. Llanes, G.R. No. 25386, October 20, 1926*)
- He who claims exemption should prove his factual and legal basis for exemption. (*CIR vs. Acesite Philippines Hotel Corporation, G.R. No. 147295, February 16, 2007*)
- Tax exemptions are strictly construed against the person claiming it. (*Esso Standard Eastern, Inc. vs. Acting Commissioner of Customs, GR No. L-21841, October 28, 1966*)

Nature of Tax Exemption

- It is a personal privilege of the grantee.
- It is generally revocable by the government unless the exemption is founded on a contract, which is protected from impairment, but the contract must contain the other essential elements of contracts.
- It implies a waiver on the part of the government to collect what otherwise would be due, and in this sense is prejudicial thereto.
- It is not necessarily discriminatory so long as the exemption has a reasonable foundation or rationale basis.

Exempt Person	Exempt Transaction
As to Nature	
Refers to an individual or entity that is exempt from tax liability due to specific qualifications or status.	Refers to a specific activity or type of transaction that is exempt from taxation, regardless of the status of the taxpayer.
As to Scope	
The exemption can cover a wide range of transactions if the law intends to apply the exemption broadly due to the taxpayer's status.	Applies only to specific transactions, meaning the exemption is not based on the taxpayer's identity but rather the activity being conducted.
As to Effect	
Any taxpayer who enters into an exempt transaction is eligible for the exemption, irrespective of whether they are typically subject to tax	Exempt transactions can benefit any taxpayer engaging in the activity as long as the statutory requirements are met.

ii. Express or Implied - A grant of immunity, express or implied, to particular persons or corporations from the obligation to pay taxes. (*Surigao Consolidated Mining vs. CIR, G.R. No. L-14878, December 26, 1963*)

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*(Casanovas vs. Hord, G.R. No. 3473,
March 22, 1907)*

Express	Implied
Expressly granted by the Constitution, statutes, treaties, franchises or similar legislative acts.	When particular persons, properties, or exercise are deemed exempt as they fall outside the scope of the taxing provision itself.

iii. Contractual

Those agreed to by the taxing authority in contract lawfully entered into by them under enabling laws. *(Casanovas vs. Hord, G.R. No. 3473, March 22, 1907)*

Contractual tax exemptions are those agreed to by the taxing authority in contracts, such as those contained in government bonds or debentures, lawfully entered into by them under enabling laws in which the government, acting in its private capacity, sheds its cloak of authority and waives its governmental immunity. Truly, tax exemptions of this kind may not be revoked without impairing the obligations of contracts.

These contractual tax exemptions, however, are not to be confused with tax exemptions granted under franchises. A **franchise** partakes the nature of a grant which is beyond the purview of the non-impairment clause of the Constitution. Article XII, Section 11, of the 1987 Constitution is explicit that no franchise for the operation of a public utility shall be granted except under the condition that such privilege shall be subject to amendment, alteration or repeal by Congress as and when the common good so requires. *(Meralco vs. Province of Laguna, G.R. No. 131359, May 5, 1999)*

Examples of contractual tax exemptions

These examples are protected by the non-impairment clause:

- i. Government bonds or debentures
- ii. Perfected mining concession granted by the Spanish Government.

Rationale/Grounds for Exemption

Being a waiver from its power to tax, the government, in granting tax exemption, should justify that the grant of such exemption will benefit the body of people, which is sufficient to offset the loss of revenue occasioned thereby.

Grounds for Tax Exemption

i. Contract – the grant of tax exemption is usually contained in the charter of the corporation to which the exemption is granted.

ii. Public policy -to encourage new and necessary industries, or to foster charitable institutions.

iii. Reciprocity – to reduce the rigors of international double or multiple taxation, tax exemptions may be granted in treaties. A tax exemption is a personal privilege of the grantee and therefore not assignable; it is generally revocable by the government, unless founded on contract and must not be discriminatory.

iv. Construction of Tax Exemption

Taxation is the rule and exemption is the exception.

The burden of proof rests upon the party claiming exemption to prove that it is, in fact, covered by the exemption so claimed. Hence, as a rule, tax exemptions are construed strongly against the claimant. Exemptions must be shown to exist clearly and categorically, and supported by clear legal provision.

Tax refunds are in the nature of tax exemptions and are likewise strictly construed against the taxpayer. *(Davao Gulf Lumber Corp. vs. CIR, G.R. No. 117359, July 23, 1998)*

Tax exclusions (removal of otherwise taxable items from the reach of taxation) are likewise strictly construed against the taxpayer. *(Smart*

ARELLANO UNIVERSITY SCHOOL OF LAW BAR OPERATIONS COMMISSION 2025

Communications, Inc. vs. City of Davao, G.R. No. 155491, September 16, 2008)

offer in the settlement of the original claim.

The strict construction against tax exemptions also mandates withholding agents to strictly observe the proper procedure to withhold tax when obligated to do so. (*National Development Company vs. CIR, G.R. No. L-53961, June 30, 1987*)

v. Revocation of Tax Exemption

If the grant of an exemption does not constitute a contract, but merely "a spontaneous concession by the legislature, not connected with any service or duty imposed" it is REVOCABLE by the power which made the grant.

Thus, if the basis of the tax exemptions is by virtue of a franchise granted by Congress, the exemption may be revoked. However, if the tax exemption constitutes a binding contract and for a valuable consideration, the government cannot unilaterally revoke the tax exemption.

10. COMPROMISE AND TAX AMNESTY

Compromise

A **compromise** is a contract whereby the parties, by making reciprocal concessions, avoid litigation or put an end to one already commenced. (*Article 2028, New Civil Code*).

In a tax compromise, the Bureau of Internal Revenue (BIR) and the taxpayer agree to settle the tax liability for a reduced amount. (Sec. 204 A, NIRC)

For a valid tax compromise to occur, the following requisites must be met:

1. The taxpayer must have a tax liability.
2. There must be an offer (by the taxpayer or the Commissioner) of an amount to be paid by the taxpayer.
3. There must be an acceptance (by the Commissioner or the taxpayer) of the

Persons Allowed to Enter into Compromise of Tax Obligations:

1. BIR Commissioner – as expressly authorized by the NIRC subject to the following conditions.

- a) When a reasonable doubt as to validity of the claim against the taxpayer exist; OR
- b) The financial position of the taxpayer demonstrates a clear inability to pay the assessed tax. (*Sec. 204, NIRC*)

2. Collector of Customs- with respect to custom duties limited to cases where the legitimate authority is specifically granted such in remission of duties. (*Sec. 709, Tariffs and Customs Code*)

3. Customs Commissioner- subject to the approval of the Secretary of Finance, in cases involving the imposition of fines, surcharges, and forfeitures. (*Sec. 2316, Tariffs and Customs Code*)

The following are the grounds for a tax compromise offer:

1. **Doubtful validity of the assessment** - when there exists reasonable doubt as to the validity of the claim against the taxpayer (e.g., one arising from a jeopardy assessment, arbitrary assessment)
2. **Financial incapacity** - when the financial position of the taxpayer demonstrates a clear inability to pay the assessed tax.

NOTE: The Commissioner of Internal Revenue (CIR) has the authority to compromise the payment of any internal revenue tax on these grounds subject to a minimum rate

Minimum Compromise Rates

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Compromise agreements have minimum payment rates, which vary depending on the reason for the compromise. These minimum percentages help ensure the government receives a reasonable portion of the owed taxes, even when agreeing to a reduced settlement. The rates are based on the ground of the tax compromise offer:

- **Financial Incapacity:** *At least 10%* of the basic assessed tax (excluding penalties and interest)
- **Doubtful Validity:** *At least 40%* of the basic assessed tax (excluding penalties and interest).

If the original tax amount (excluding penalties and interest) is greater than ₱1,000,000.00, or if the proposed settlement is below the required minimum percentage, the compromise agreement must be approved by an Evaluation Board which consists of the Commissioner of Internal Revenue and the four Deputy Commissioners.

Allowed Tax Compromise vs Prohibited Tax Compromise

Tax compromise may be allowed in the following cases:

1. Delinquent accounts;
2. Tax cases under administrative protest after the taxpayer received the Final Assessment Notice (FAN), if handled within the BIR National Office Units (e.g., Regional Offices, Revenue District Offices, Legal Service, Large Taxpayer Service, Collection Service, Enforcement Service, or others).
3. Civil tax cases being disputed before the courts;
4. Collection cases filed in courts;
5. Criminal violations, *except*:
 - i. Those already filed in court; or
 - ii. Those involving criminal tax fraud

Tax compromise is not allowed in the following cases:

1. Withholding tax cases *except* when the applicant-taxpayer invokes provisions of law that cast doubt on the taxpayer's obligation to withhold;
2. Criminal tax fraud cases confirmed by the CIR or his duly authorized representative;
3. Criminal violations filed in court;
4. Delinquent accounts with duly approved schedule of installment payments;
5. Cases where the original tax assessment has been reduced following a reinvestigation or reconsideration, and the taxpayer consents to the amount by signing required agreement form.
6. Cases that have become final and executory after a court judgment *may* be considered for compromise if the taxpayer argues the original assessment was invalid.
7. Estate Tax cases wherein the taxpayer has the financial inability to pay.

Other protested cases, not specifically included, will be handled by the Regional or National Evaluation Board on a case-by-case basis.

Tax Amnesty

Tax amnesty is a general pardon or intentional overlooking by the State of its authority to impose penalties on persons otherwise guilty of evasion or violation of a revenue or tax law. It partakes of an absolute forgiveness or waiver by the government of its right to collect what is due it and to give tax evaders who wish to relent a chance to start with a clean slate. A tax amnesty, much like a tax exemption, is never favored nor presumed in law. The grant of a tax amnesty, similar to a tax exemption, must be construed strictly against the taxpayer and liberally in favor of the taxing authority. (*CIR vs. Philippine-Aluminum Wheels, Inc., G.R. No. 216161, August 9, 2017*)

A tax amnesty is a general pardon or the intentional overlooking by the State of its authority to impose penalties on persons

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otherwise guilty of violating a tax law. It partakes of an absolute waiver by the government of its right to collect what is due it and to give tax evaders who wish to relent a chance to start with a clean slate. A tax amnesty, much like a tax exemption, is never favored or presumed in law. The grant of a tax amnesty, similar to a tax exemption, must be construed strictly against the taxpayer and liberally in favor of the taxing authority. (*Asia International Auctioneers, Inc. vs. CIR, G.R. NO. 179115, September 2012*)

Distinguish Tax Amnesty from Tax Exemption

Tax Amnesty	Tax Exemption
Immunity from all criminal and civil obligations from non-payment of taxes.	Immunity from civil liability only.
It is a general pardon given to all taxpayers.	Immunity or privilege granted to qualified taxpayers from a charge or burden of which others are subjected. (<i>Florer vs. Sheridan, 137 Ind. 28, 36 NE 365</i>)
It applies only to past tax periods. (<i>People vs. Castañeda, G.R. No. L-46881, September 15, 1988</i>)	Applies prospectively after the grant of the exemption or from qualification therefrom.

(*Soriano, Manuel and Laco, The Tax Reviewer, 2021 Edition, pp. 11-12*)

11. Taxpayer's Suit: Rationale and Requisites

Nature of Taxpayer Suit

A taxpayer is allowed to sue where there is a claim that public funds are illegally disbursed, or that the public money is being deflected to any improper purpose, or that there is wastage of public funds through the enforcement of an invalid or unconstitutional law. A person suing

as a taxpayer, however, must show that the act complained of directly involves the illegal disbursement of public funds derived from taxation. He must also prove that he has sufficient interest in preventing the illegal expenditure of money raised by taxation and that he will sustain a direct injury because of the enforcement of the questioned statute or contract. (*Syjuco, Jr. vs. Abayan, G.R. Nos. 215650, 215653, 215703, 215704 & 216735, March 28, 2023*).

When the disposition is of alleged public property (like paintings and silverware of the Marcoses) and not of public funds, a taxpayer's suit is improper. (*Joya vs. Presidential Commission on Good Government, G.R. No. 96541, August 24, 1993*)

When no public funds were disbursed or spent (such as when Special Elections were not held, and thus, nothing was spent), a taxpayer's suit is improper. (*Lozada vs. COMELEC, G.R. No. L-59068, January 27, 1983*)

When what is questioned is a contract entered into by a government-owned or -controlled corporation (GOCC) wherein public funds will be used, then a taxpayer's suit is proper. (*Abaya vs. Ebdane, G.R. No. 167919, February 14, 2007*)

By invoking "transcendental importance", "paramount public interest", or "far-reaching implications", ordinary citizens and taxpayers have been allowed to sue even if they failed to show direct injury. The Court then noted that in cases where serious legal issues were raised or where public expenditures of millions of pesos were involved, the Court had liberally upheld the standing of taxpayers. (*Mamba vs. Lara, GR. No. 165109, 14 December 2009*)

Requisites of Taxpayer's Suit

1. Public funds are disbursed by a political subdivision or instrumentality, and in doing so, a law is violated or some irregularity is committed, and

ARELLANO UNIVERSITY SCHOOL OF LAW BAR OPERATIONS COMMISSION 2025

2. The petitioner is directly affected by the act.
(*Bayyo Association, Inc. vs. Tugade*, G.R. No. 254001, July 11, 2023)

Section 23 of the NIRC provides individuals and corporations subject to income tax as follows:

B. NATIONAL INTERNAL REVENUE CODE OF 1997 (NIRC), as amended

1. INCOME TAX

a. NATURE AND GENERAL PRINCIPLES

Definition of Income Tax

Income tax is imposed on an individual or entity as a form of excise tax or a tax on the privilege of earning income. In exchange for the protection extended by the State to the taxpayer, the government collects taxes as a source of revenue to finance its activities. (*Maynilad Water Services, Inc. vs. National Water and Resource Board*, G.R. Nos. 181764, 187380, 207444, December 7, 2021)

i. Criteria in Imposing Philippine Income Tax

(a) Citizenship Principle

The basis of the imposition of income tax is the taxpayer's citizenship.

All citizens of the Philippines, whether resident or non-resident, are subject to our income tax. (*Empesando vs. CIR*, CTA Case No. 9093 dated July 20, 2020)

(b) Residence Principle

The basis of the imposition of all income tax is the residence of the taxpayer.

All income derived by an individual or entity shall be taxable in the Philippines should said individual or entity reside in the Philippines (*Id.*)

(c) Source Principle

All income derived from sources within the Philippines shall be subject to income tax.

ii. Types of Philippine Income Taxes

- a) Graduated Income Tax on Individuals
- b) Optional Income Tax of 8% on Individuals
- c) Normal Corporate Income Tax
- d) Minimum Corporate Income Tax (MCIT)
- e) Special Income Tax on Certain Corporations
- f) Final Withholding Tax (FWT)
- g) Fringe Benefits Tax (FBT)
- h) Capital Gains Tax (CGT)

iii. Kinds of Taxpayers – Individuals, Corporations, Trust, Estates

A. Based on the Income derived within the Territorial Jurisdiction of Taxing Authority

(a) Individual

1. Citizens

Resident Citizen

Individuals who are citizens of the Philippines and whose residence is within the Philippines.

Coverage: Taxable on all income derived from sourced **with and without** the Philippines [*Sec 23 (A), NIRC*] and following the semi-global/semi-schedular tax system, the applicable tax rate shall depend on the classification of the income received, whether it is compensation income, professional or business income, passive income or capital gains.

Non-resident Citizens

Section 22(E) of NIRC, as amended provides who are non-resident citizens:

- (1) A citizen of the Philippines who establishes to the satisfaction of the Commissioner the fact

ARELLANO UNIVERSITY SCHOOL OF LAW BAR OPERATIONS COMMISSION 2025

of his physical presence abroad **with a definite intention to reside therein.**

(2) A citizen of the Philippines who leaves the Philippines during the taxable year to reside abroad, either as an **immigrant** or for **employment on a permanent basis.**

(3) A citizen of the Philippines who works and derives income from abroad and whose employment thereat requires him **to be physically present abroad most of the time during the taxable year.**

(4) A citizen who has been previously considered as nonresident citizen and who arrives in the Philippines at any time during the taxable year to reside permanently in the Philippines shall likewise be treated as a nonresident citizen for the taxable year in which he arrives in the Philippines with respect to his income derived from sources abroad until the date of his arrival in the Philippines.

(5) The taxpayer shall submit proof to the Commissioner to show his intention of leaving the Philippines to reside permanently abroad or to return to and reside in the Philippines.

Individuals considered as nonresident citizens

(1) Immigrant - one who leaves the Philippines to reside abroad as an immigrant for which a foreign visa has been secured.

(2) Permanent employee - one who leaves the Philippines to reside abroad for employment on a more or less permanent basis.

(3) Contract worker - one who leaves the Philippines on account of a contract of employment which is renewed from time to time under such circumstance as to require him to be physically present abroad most of the time (not less than 183 days).

Nonresident citizens who are exempt from tax with respect to income derived from sources outside the Philippines shall no longer be required to file information returns from sources outside the Philippines. (*R.R. No. 5-2001*)

The phrase "most of the time"

Works and derives income from abroad and whose employment thereat requires him to be physically present abroad most of the time during the taxable year. To be considered physically present abroad **most of the time** during the taxable year, a contract worker must have **outside the Philippines for not less than 183 days** during such taxable year. (*Sec. 2, R.R. 1-79*)

Shall mean that the said citizen shall have stayed abroad for **at least 183 days in a taxable year.** However, citizens who work outside of the Philippines for at least 183 days in a taxable year due to a contract of employment with a Philippine employer (such as employees seconded to a foreign country) **are not considered nonresident citizens** because they are not considered employed abroad. They do not fall within Section 22(E)(3) because their employment remains with the Philippine employer. (*BIR Ruling No. 116-12*)

Employees who rendered services for more than 183 days in foreign countries **were not** considered non-residents on the basis that: (1) the employee-employer relationship continued to exist between the local company and employees; and (2) the salaries of the employees were paid by the local company. (*BIR Ruling No. 517-2011*)

NOTE: The term 'residence' is to be understood not in its common acceptance as referring to 'dwelling' or 'habitation,' but rather to 'domicile' or legal residence, that is, 'the place where a party actually or constructively

ARELLANO UNIVERSITY SCHOOL OF LAW BAR OPERATIONS COMMISSION 2025

has his permanent home, where he, no matter where he may be found at any given time, eventually intends to return and remain (*animus manendi*). (*Japzon vs. COMELEC, G.R. No. 180088, January 19, 2009*)

Overseas contract worker (OCW) or overseas Filipino worker (OFW)

An individual citizen of the Philippines who is working and deriving income from abroad as an overseas contract worker or a seaman is taxable only on income derived from sources within the Philippines provided that a seaman who is a citizen of the Philippines and who receives compensation for services rendered abroad as a member of the complement of a vessel engaged exclusively in international trade shall be treated as an overseas contract worker. (*Sec 23(C), NIRC*)

An OCW of an OFW's income arising out of his overseas employment is exempt from income tax. However, if an OCW or OFW has income earnings are subject to Philippine income tax. (*Revenue Regulations No. 01-2011*)

Coverage: Taxable only on income derived from sourced **within** the Philippines [*Sec 23 (B), NIRC*] and generally subject to the same tax rates as resident citizens.

2. Aliens

Resident Alien

An individual whose residence is within the Philippines and are not citizens.

An alien is considered as resident if:

- (1) He is not a mere transient or sojourner (*R.R. No. 02-40, Sec. 5*);
- (2) He has no definite intention as to his stay in the Philippines; or
- (3) His purpose is of such nature that an extended stay may be necessary for its

accomplishment and to that end, the alien makes home temporarily in the Philippines (*BIR DA -ITAD Ruling No. 153-06*)

When is residency lost?

A resident alien who has acquired residence in the Philippines retains his status as a resident alien until he abandons the same and departs the Philippines. Mere intention to change his residence is not enough. (*Sec. 5, R.R. No. 02-40*)

Coverage:

Taxable only on income sourced **within** the Philippines and generally taxed in the same manner as non-resident citizens.

Non-Resident Alien Engaged in Trade or Business

There are two types of income taxpayers of this kind:

- (1) Those actually conducting or business in the Philippines.
- (2) A non-resident alien individual who shall come to the Philippines and stay therein for an aggregate period of more than 180 days during any calendar year. (*Sec. 25[A][1], NIRC*)

Coverage:

Taxable only on income received from sources **within** the Philippines and generally taxed in the same manner as resident aliens.

Non-Resident Alien Not Engaged in Trade or Business

A non-resident alien is not engaged in trade of business if the period of his stay in the Philippines does not exceed 180 days.

Coverage:

Taxable only on income received from sources **within** the Philippine. However, they are taxed differently in that their income is not classified in accordance with the semi-global/semi-schedular tax system.

ARELLANO UNIVERSITY SCHOOL OF LAW BAR OPERATIONS COMMISSION 2025

They are subject to a **final withholding tax of 25%** on their **entire income** from sources within the Philippines, such as:

- Salaries, wages, compensation, remuneration, and emoluments;
- Interests, premiums, annuities, rents;
- Cash and property dividends; and
- Other fixed and determinable annual or periodic casual gains.

Exception:

Capital gains from sale of shares of stock in domestic corporation and real property located in the Philippines shall be subject to the income tax prescribed for citizens and resident aliens.

3. Special Aliens

The following individuals are considered as special aliens:

(a) Employed by Regional or Area Headquarters and Regional Operating Headquarters of Multinational Companies (*Sec. 25(C), NIRC*)

(b) Employed by Offshore Banking Units (*Sec. 25(D), NIRC*)

(c) Employed by Petroleum Service Contractor and Subcontractor (*Sec. 25(E), NIRC*)

All concerned employees of regional or area headquarters and regional operating headquarters of multinational companies, offshore banking units and petroleum service contractor and subcontractor shall be subject to the regular tax rate. (*RR No. 8-2018*)

Respective incomes of alien individuals employed by the abovementioned entities are **now similarly taxed as income of regular employees of locally established entities**. As such, these alien individuals are subject to the same administrative requirements of the BIR being imposed on other regular employees, such as substituted filing, issuance

of BIR Form 2316 and inclusion in the monthly withholding tax remittance on compensation and in the prescribed alphalists. (*RMC No. 116-2019*)

Further, alien individuals employed by foreign principals and assigned to render services exclusively to these local entities, otherwise known as "seconded employees or secondees," are **likewise subject to regular income tax rates**. It is grounded on the principle of situs of taxation, considering that the services rendered by these alien individuals are performed in the Philippines, regardless of whether their salaries are being paid by the foreign principals or advanced by these local entities. (*Id.*)

Coverage:

Taxable income received from all sources within the Philippines shall be subject to income tax in the same manner as a citizen and resident alien.

4. Alien Employees of POGO and Offshore Gaming Operation

Foreign nationals or non-Filipino citizens regardless of their resident and class of working employment permit or visa who are employed and assigned in the Philippines by an OGL or its Accredited Service Provider. (*Sec. 25(G), NIRC*)

Coverage:

(1) Shall be subject to 25% final withholding tax on the gross income or PhP 12,500 per month, whichever is higher.

NOTE: Gross income shall include, whether in cash or in kind, basic salary/wages, annuities, compensation, remuneration, and other emoluments such as honoraria and allowances, received by the alien employee from a POGO entity.

ARELLANO UNIVERSITY SCHOOL OF LAW BAR OPERATIONS COMMISSION 2025

(2) Any income earned from all other sources within the Philippines by foreign employees shall be subject to the income tax under the pertinent provisions of NIRC, as amended.

(b) Corporations

Corporations shall include one-person corporations, partnerships, no matter how created or organized, joint-stock companies, joint accounts (*cuentas en participacion*), associations, or insurance companies.

A **one-person corporation** is a corporation with a single stockholder. Provided, that only a natural person, trust, or an estate may form a one-person corporation. (*Sec. 2 (a) Rev. Reg. No. 5-2021*)

Exclusions:

General professional partnerships and joint ventures or consortiums formed for the purpose of undertaking construction projects or engaging in petroleum, coal, geothermal and other energy operations pursuant to an operating consortium agreement under service contract with the Government.

1. Domestic Corporation

A corporation created and organized in the Philippines or under its laws (*applying the law of incorporation test*) (*Sec. 22 [c], NIRC, as amended*).

Coverage:

Regular Corporate Income Tax

(1) All other domestic corporations, in general shall be subjected to income tax rate of twenty-five percent **(25%)** effective July 1, 2020, on taxable income derived during each taxable year **from all sources within and without the Philippines.**

(2) Domestic corporations with:

- **Net taxable income not exceeding** five million pesos **(P5,000,000.00)** and

- **Total assets not exceeding** One hundred million pesos **(P100,000,000.00)**, excluding land where the business office, plant, and equipment are situated shall be taxed at twenty percent **(20%)**. (*Sec. 27 (A), NIRC*)

Minimum Corporate Income Tax

The MCIT is 2% of the gross income. (*Secs. 27(E)(1) and 28(A)(2), NIRC*)

The MCIT is imposed **beginning on the fourth taxable year immediately following the year in which such corporation commenced its business operations**, when it is greater than the regular income tax computed for the taxable year. (*Sec. 3 of RR No. 5-2021 dated April 8, 2021*)

For purposes of the MCIT, the taxable year in which business operations commenced shall be the year in which the domestic corporation registered with the BIR. (*RR No. 9-1998, August 25, 1998*)

Under RR No. 4-95, the date of commencement of operations of thrift banks is the date the particular thrift bank was registered with the SEC or the date when the Certificate of Authority to Operate was issued to it by the Monetary Board of the BSP, whichever comes later. (*Manila Banking Corporation vs. CIR, GR No. 168118 dated August 28, 2006*)

2. Resident Foreign Corporation

Foreign Corporation which are engaged in trade or business in the Philippines (*Section 22 (H), NIRC*)

A corporation organized, authorized, or existing under the laws of any foreign country engaged in trade or business in the Philippines. (*Sec. 2 (g) Rev. Reg. No. 5-2021*)

Coverage:

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Taxable only on income derived from sources **within** the Philippines.

"Doing Business"

Republic Act No. 7042 or the Foreign Investments Act of 1991, "doing business" includes any act that imply a continuity of commercial dealings or arrangements, and which contemplate the performance of functions normally incident to and in progressive prosecution of commercial gain, such as soliciting orders and service contracts; opening offices, whether called liaison offices or branches; appointing representatives or distributors domiciled in the Philippines; staying in the country for 180 aggregate days or more; and participating in the management of any domestic business. It shall not include:

- Mere investment as a shareholder in a domestic corporation and the exercise of rights as such investor, or having a nominee director or officer to represent its interest in a domestic corporation;
- Appointment of a representative or distributor domiciled in the Philippines which transacts business in its own account.
- There is no specific criterion as to what constitutes "doing," or "engaging in," or "transacting" business." The term implies a continuity of commercial dealings and arrangements and contemplates, to that extent, the performance of acts or works or the exercise of some of the functions normally incident to and in progressive prosecution of commercial gain or for the purpose and object of the business organization. (*CIR vs British Overseas Airways Corporation, G.R. Nos. L-65773-74, April 30, 1987*)

In order for a foreign corporation. to be regarded as doing business within a State, **there must be continuity of conduct and intention to establish a continuous business**, such as the appointment of a local

agent, and not one of a temporary character. (*Id.*)

3. Non-Resident Foreign Corporation

Foreign Corporation which are not engaged in trade or business in the Philippines (*Section 22 (I), NIRC*)

Coverage:

Taxable only on income received from sources **within** the Philippine. However, they are taxed differently in that their income is not classified in accordance with the semi-global/semi-schedular tax system.

They are subject to a **final withholding tax of 25%** on their **entire income** from sources within the Philippines, such as:

- Interests, annuities, rents and royalties;
- Dividends
- Premiums, except reinsurance premiums; and
- Other fixed and determinable annual or periodic casual gains.

Exception:

A final tax at the rate of 15% is imposed upon the net capital gains realized during the taxable year from the sale, barter, exchange or other disposition of shares of stock in a domestic corporation, except shares sold, or disposed of through the stock exchange. The latter is subject to the 0.006% stock transaction tax instead of income tax. (*Section 28(B)(5)(c), NIRC*)

4. Partnership

Partnership are subsumed under the term "corporation". They are taxed in the same manner as a corporation, regardless of how they are created or organized, and whether they are registered or not. Thus, partnership income is subject to corporate income tax, and the individual partners' tax, and the individual partners' distributive shares are treated and taxed as dividends.

ARELLANO UNIVERSITY SCHOOL OF LAW BAR OPERATIONS COMMISSION 2025

Under Section 73(D) of the NIRC, as amended, such shares "shall be deemed to have been actually or constructively received by the partners in the same taxable year and shall be taxed to them in their individual capacity, whether actually distributed or not."

General professional partnerships

Formed by persons for the sole purpose of exercising their common profession, therefore no part their income is derived from engaging in trade or business. They are not taxable partnerships subsumed under the term "corporation."

A general professional partnership is not a taxable entity because it is no more than a mechanism or a flow-through entity in the generation of income by, and the ultimate distribution of such income to, each of its individual partners. (*Tan vs Del Rosario, G.R. No. 109289, October 3, 1994*)

As such, a general professional partnership by itself is not subject to income tax. It is the individual partners comprising the same who are liable for income tax on their separate capacities. Each partner of a general professional partnership is required to report as income his distributive share, actually or constructively received, in the net income of the partnership.

5. Joint ventures

Covered by the term corporation under the NIRC, as amended, with the exception of the following:

- (a) those formed for the purpose of undertaking construction projects; and
- (b) those engaging in petroleum and energy operations, pursuant to an operating consortium agreement under a service contract with the Government.

Characteristics of Joint Venture

- (a) Contribution by its partners or members, whether capital or industrial;
- (b) Sharing of profits;
- (c) Joint proprietary interest; and
- (d) Single business transaction.

6. Co-ownership

A co-ownership is not a taxable entity, provided that the activities of the co-owners are limited to the preservation of the co-owned property and the collection of income therefrom. Each co-owner shall be taxed individually on their respective share.

The moment, however, co-owners allow their property or income from the co-ownership to be used as a common fund for business transactions with the intention of deriving profit to be shared by them, an unregistered partnership is formed. An unregistered partnership is taxable as a corporation. (*Ona vs CIR, G.R. No. L-19342, May 25, 1972*)

(c) Estates and Trusts

Estate refers to the mass of all property, rights and obligations of a person which are not extinguished by their death. (*RR No. 13-1999*)

On the other hand, a person who establishes a **trust** is called the trustor; one in whom confidence is reposed as regards property for the benefit of another person is known as the trustee; and the Person for whose benefit the trust has been created is referred to as the beneficiary (*Article 1440, New Civil Code*)

When may the estate and the trust may be considered as separate taxpayers:

- Estate: under judicial settlement, whether testamentary or intestate
- Trust: accumulation of income, whether for (1) unascertained person/s, (2) persons with contingent interest and (3) unborn

ARELLANO UNIVERSITY SCHOOL OF LAW BAR OPERATIONS COMMISSION 2025

persons (*Section 210 and Section 61 (A), NIRC; RR No. 2-1940*)

Exceptions:

Taxable estates and trust are taxed in the same manner and on the same basis as in the case of an individual. They are also entitled to claim the same allowable deductions as in the case of individuals.

Additional deductions includes (1) income to be distributed currently by the fiduciary to the beneficiaries, (2) Part of taxable income of beneficiaries and (3) Income properly paid to any legatee, heir, or beneficiary.

Where, in the case of two or more trusts, the creator of the trust and the beneficiary in each instance is the same, the taxable income of all the trusts shall be consolidated and the tax computed on such consolidated income. (*Ingles, Tax Made Less Taxing: A Reviewer with Codals and Cases, 2021 Edition, p. 128*)

A. Based on the Amount of Gross Sales

Under RA 11976, paragraph B of Section 21 of the NIRC, as amended, was "added" as follows:

For purposes of responsive tax administration, taxpayers shall be classified as follows:

Group	Gross Sales
Micro	Less than 3M
Small	3M to less than 20M
Medium	20M to less than 1B
Large	1B

These categories shall apply to all types of taxpayers (individuals, estates, trusts, corporations, partnership, joint ventures, etc.).

Gross Sales under these categories shall refer to:

a. Total sales revenue, net of vat, if applicable, during the taxable year, without any other deductions; and

b. Business income, excluding compensation income earned under employer-employee relationship, passive income under Sections 24, 25, 27 and 28, and income excluded under Section 32(B), all of the NIRC, as amended. Business income shall include income from the conduct of trade or business or the exercise of a profession.

Purpose of Grouping

Taxpayers as Micro, Small, Medium and Large:

a. Responsive tax administration.

b. Provide certain tax concessions to Micro and Small taxpayers, such as the following civil penalties and other concessions:

- Reduced surcharge rate to 10% surcharge;
- Reduced interest rate to 6% interest;
- Reduced to P500 the penalty for failure to file certain information returns;
- Reduced compromise penalty rate to 50% on violations invoicing/printing of invoices)
- Income Tax Return (ITR) was reduced to two (2) pages only

(a) Individual vs Corporate Income Taxation – Schedular vs Flat rate

Income Tax System

There are generally two kinds of income tax systems

1. Global Tax System

The entire income of the taxpayer is aggregated and is subjected to a singular tax rate, regardless of the differences in the source or character of income earned.

2. Schedular tax system

Each source or character of income is subject to a separate and distinct kind of tax.

The Philippine income tax system is a **semi-global, semi-schedular tax system**.

ARELLANO UNIVERSITY SCHOOL OF LAW BAR OPERATIONS COMMISSION 2025

Income Tax on Individuals, Estates, and Trust

Characteristics of Individual Income Tax

1. National Tax - it is imposed by the national government
2. Progressive Tax - the individual income tax rate increases as the annual taxable income increases.
3. Capital gains tax rates and final income tax rates are proportional.
4. Ad valorem Tax - the tax base is the taxable income.
5. Privilege/Transactional Tax - it is a tax imposed on the income-earning transaction
6. Direct Tax - there is no tax shifting involved

Individuals are classified either as:

1. Compensation Income Earners;
2. Purely self-employed individuals and/or professionals;
3. Mixed Income Earners (*Section 24, NIRC as amended*)

Situs Rules

Taxpayer	Taxable on Income from Sources	
	Within the PH	Without the PH
Individual		
Resident Citizen	Yes	Yes
Non-resident Citizen	Yes	No
Resident Alien		
Non-resident Alien Engaged in Trade or Business		
Non-resident Alien not Engaged in Trade or Business		

Regular Income Tax on Individuals

General rule: All items of taxable income that are not subject to either final income tax or

capital gains tax are subject to regular income tax.

Items subject to regular income tax may be subject to creditable withholding tax.

Kinds of Regular Income Tax for Individuals

a. Graduated Income Tax Rates

Annual Taxable Income is over	But not over	Tax shall be	Plus	Of excess over
	250,000		0%	
250,000	400,000		20%	250,000
400,000	800,000	30,000	25%	400,000
800,000	2,000,000	130,000	30%	800,000
2,000,000	8,000,000	490,000	32%	2,000,000
8,000,000		2,410,000	35%	

With the above income tax tables, the first PhP250,000 annual income taxable income of an individual taxpayer is **exempt from income tax**.

Pursuant to the principle of theoretical justice, it can be said that this amount is what Congress considers as the basic amount an individual spends for sustaining one's life and is therefore, protected from reach of the power of taxation

b. 8% Income Tax Option

Individuals, particularly self-employed individuals/ professionals (*Section 24 (A)(2)(b), NIRC, as amended*) and mixed income earners (*Section 24 (A)(2)(c), NIRC, as amended*) can avail of this option.

Requisites of 8% Income Tax Options:

1. The individual should not be VAT-registered (*RMC No. 50-2018*)
2. The individual's annual gross sales or receipts should not exceed P3,000,000

The 8% income tax option is in lieu of graduated income tax and percentage tax. It is availed at or prior to the filing of the first quarter income tax return. Once availed, such

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choice is irrevocable for the rest of the year.
(Q19/A19, RMC No. 50-2018)

Tax Base

Self-Employed Individual	Mixed Income Earner
Gross Sales or gross receipts and other non-operating income in excess of P250,000	Gross sales or gross receipts and other non-operating income

Persons not Qualified to Avail of the 8% Income Tax Option

i. Purely compensation income earners

Compensation is always subject to graduated income tax rates. Further, the 8% income tax option contemplates the existence of gross sales, which a purely compensation income earner cannot generate.

ii. VAT-registered taxpayers, regardless of the amount of gross sales/ receipts and other non-operating income.

iii. Non-VAT taxpayers whose gross sales/ receipts and other non-operating income exceeded the P3,000,000 VAT threshold

This is considering that they are already required to register as a VAT-registered taxpayer.

iv. Taxpayers who are subject to Other Percentage Taxes under Title V of the Tax Code, as amended, except those under Section 116 of the same title.

If an entity is subject to percentage taxes, except the 3% percentage tax, then that taxpayer can no longer avail of the 8% income tax option. For instance, if a taxpayer is subject to the amusement tax, franchise tax, or overseas communications tax, then the taxpayer is no longer entitled to the 8% income tax option. This is because the 8% income tax option is in lieu of percentage taxes. To allow a taxpayer subject to percentage taxes, the

rates of which are oftentimes higher than the 3% percentage tax imposed under Section 116, would result to a reduction in tax collections by the government. Applying the example earlier, the 8% income tax cannot be said to be in lieu of the 30% amusement tax.

v. Partners of a General Professional Partnership (GPP) since their distributive share from the GPP is already net of costs and expenses.

Note that a partner of a commercial partnership is still allowed to avail of the 8% income tax rate if such partner has income from the conduct of trade or business and practice of profession.

vi. Individuals enjoying income tax exemption such as those registered under the Barangay Micro Business Enterprises (BMBEs), etc., since taxpayers are not allowed to avail of double or multiple tax exemptions under different laws, unless specifically provided by law. (Q16/A16, RMC No. 50-2018)

Income Tax on Corporation

Situs Rules

Taxpayer	Taxable on Income from Sources	
	Within the PH	Without the PH
Corporation		
Domestic Corporation	Yes	Yes
Resident Foreign Corporation	Yes	No
Non-resident Foreign Corporation		

Characteristics of Corporate Income Tax

1. National Tax - it is imposed by the national government

2. Proportional Tax - the corporate income tax rate remains constant regardless of the change

ARELLANO UNIVERSITY SCHOOL OF LAW BAR OPERATIONS COMMISSION 2025

in tax base, except for the special rate available for corporations not exceeding the large-entity threshold

3. Ad valorem Tax - the tax base is the taxable income.
4. Privilege/Transactional Tax - it is a tax imposed on the income-earning transaction
5. Direct Tax - there is no tax shifting involved

Regular Corporate Income Tax

General rule: All items of taxable income that are not subject to either final income tax or capital gains tax are subject to regular income tax.

Items subject to regular income tax may be subject to creditable withholding tax.

Regular Taxation of Domestic and Resident Foreign Corporations

The higher between the:

- A. Regular Corporate Income Tax; and

Corporate Taxpayer	Tax Rate
In general, domestic and resident foreign corporation	25%
Domestic Corporation with net taxable income not exceeding 5M and total assets not exceeding 100M	20%

- B. Minimum Corporate Income Tax (MCIT) which is **2% of Gross Income**

i) Income Tax on Special Corporation

Special Corporations are taxable corporations that do not follow the regular rules of corporate income taxation and are instead subject to special rates or subject to tax based on different tax base.

i. Proprietary Educational Institutions and Non-Profit Hospitals

A proprietary educational institution is any private schools maintained and administered

by private individuals or groups, with an issued permit to operate from the Department of Education (DepEd), Commission on Higher Education (CHED), or Technical Education and Skills Development Authority (TESDA), under existing laws and regulations. (*Section 27(B), NIRC; RR No. 5-2021*)

A non-profit hospital is any private hospitals, which are non-profit, maintained and administered by private individuals or groups.⁷⁶³ To be considered as non-profit, no net income or asset accrues to or benefits any member or specific person, with all the net income or assets devoted to the institution's purposes and all its activities conducted not for profit. (*Id.*)

Income Tax on Proprietary Educational Institutions and Non-profit Hospitals

Situation	Applicable Tax Rate
In general	20%/25%
If the gross income from "unrelated trade, business or other activity" does not exceed 50% of the total gross income derived from all sources	10%

Predominance Test

Determines whether the income realized by the institution consists mainly of income from the operation of the educational institutions or hospitals.

Pursuant to this test, the preferential income tax of 10% of taxable income shall not apply if the gross income from "unrelated trade, business or other activity" exceeds 50% of the total gross income derived by such educational institutions or hospitals from all sources. In which case, the educational institutions or hospitals shall be taxed as a regular corporation subject to the regular corporate income tax or minimum corporate income tax, whichever is higher.

ARELLANO UNIVERSITY SCHOOL OF LAW BAR OPERATIONS COMMISSION 2025

In applying the predominance test, the term "unrelated trade, business or other activity" means any trade, business or other activity, the conduct of which is not substantially related to the exercise or performance by such educational institution or hospital of its primary purpose or function. (*Section 27(B), NIRC as amended, RMC No. 26-86*)

The hospital is exempt from income tax with respect to their activities conducted exclusively for charitable or social welfare purposes. An institution under Section 30(E) or (G) of the NIRC does not lose its tax exemption even if it earns income from its for-profit activities. (*CIR vs St. Luke's Medical Center, Inc., G.R. Nos. 195909, September 26, 2012*)

However, the income derived from a property or activity conducted for profit shall be subject to income tax at the rate provided under the NIRC. Here, the income of the hospital from paying patients came from an activity conducted for profit, hence, taxable. Since, the entity that earned the income is a non-profit hospital, the applicable tax is the preferential income tax of 10% of taxable income. (*Id.*)

ii. Government owned and controlled corporations

Generally, they are subject to regular income tax unless provisions of existing special or general laws provide otherwise.

Exceptions:

The following GOCCs are exempt from income tax:

1. Government Service Insurance System (GSIS);
2. Social Security System (SSS);
3. Home Development Mutual Fund (HDMF);
4. Philippine Health Insurance Corporation (PHIC), and
5. Local water districts are not subject to income tax.

Income tax on Philippine Amusement and Gaming Corporation (PAGCOR) as GOCC

PAGCOR is subject to a franchise tax of five percent (5%) of the gross revenue or earnings it derives from its operations and licensing of gambling casinos, gaming clubs and other similar recreation or amusement places, gaming pools, and other related operations as described above. On the other hand, PAGCOR is subject to regular corporate income tax for income realized from other necessary and related services. (*Section 13(2) (a) of Presidential Decree No. 1869*)

iii. Resident Foreign Corporation on Branch Profit Remittance Tax

Technically not a corporation, but is a special rate applicable to resident foreign corporation.

NOTE: It is the outbound branch profit that is subject to the tax, not the inbound profits.

Coverage:

Imposes fifteen percent (15%) tax for branch profit remittances on the total profits applied or earmarked for remittances without any deduction for the tax component thereof, in Branch profit remittance tax covers the remittance of all resident foreign corporations, including regional operating headquarters of multinational companies, foreign currency deposit units or offshore banking units of foreign banks, and international carriers, except Philippine Economic Zone Authority-registered entities. (*Section 28 (A)(5), NIRC as amended*)

Exclusions:

Interest, dividends, rents, royalties, remuneration for technical services, salaries, wages, premiums, annuities, emoluments or other fixed or determinable annual, periodic or casual gains, profits, income, and capital gains received by a foreign corporation during each taxable year from all sources within the Philippines shall not be treated as branch profit unless the same are effectively connected with the conduct of the taxpayer's trade or business in the Philippines. (*Id.*)

Effectively connected with the conduct of taxpayer's trade, or business

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Does not necessarily mean that the income must be derived from the actual operation of the taxpayer-corporation's trade or business. It is sufficient that the income arises from the business activity in which the corporation is engaged. (*RMC No. 55-80*)

iv. International Carriers

Distinguish International Air Carrier from International Sea Carrier

International Air Carrier	International Sea Carrier
A foreign airline corporation doing business in the Philippines having been granted landing rights in any Philippine port to perform international air transportation services/ activities or flight operations anywhere in the world.	a foreign shipping corporation doing business in the Philippines, having touched any Philippine port to perform international sea transportation services/ activities from the Philippines to anywhere in the world and vice versa

International carriers may be considered as online or offline carriers:

i. On-line carrier

International air or sea carriers having or maintaining flight operations to and from the Philippines or having touched any Philippine port

ii. Off-line carriers

International air carriers having no flight operations to and from the Philippines or having not touched any Philippine port.

Income Tax on International Carriers

An international carrier doing business in the Philippines shall be subjected to 2.5% on its Gross Philippines Billings. (*Section 28(A)(3), NIRC, as amended*)

Definition of Gross Philippine Billings

It pertains to **gross revenue** derived from carriage of persons, excess baggage, cargo, and mail originating from the Philippines in a continuous and uninterrupted flight, irrespective of the place of sale or issue and the place of payment of the ticket or passage document.

NOTE:

The GPB covers gross revenue derived from transportation of passengers, cargo and/or mail originating from the Philippines up to the final destination. Any other income, therefore, is subject to the regular income tax rate. (*Association of International Shipping Lines, Inc. vs. Secretary of Finance, GR No. 222239 dated January 15, 2020*)

The exclusion of demurrage and detention fees from the preferential rate of 2.5% is proper since they are not considered income derived from transportation of persons, goods and/or mail, in accordance with the rule *expressio unius est exclusio alterius*. (*Id.*)

Offline carriers are not subject to GPBT, considering that they do not have flights originating from the Philippines. (*CIR vs British Overseas Airways Corporation, G.R. No. L-65773-74, April 30, 1987*) However, they may be subject to regular corporate income tax on their sale of tickets in the Philippines by their agents. (*Id.*)

v. Regional Headquarters

Distinguish Regional or Are Headquarters (RAHQ) from Regional Operating Headquarters (ROHQ)

RAHQ	ROHQ
A branch established in the Philippines by multinational companies and which headquarters do not earn or derive income from the	A branch established in the Philippines by multinational companies which are engaged in any of the qualifying services.

ARELLANO UNIVERSITY SCHOOL OF LAW BAR OPERATIONS COMMISSION 2025

Philippines and which act as supervisory, communications and coordinating center for their affiliates, subsidiaries, or branches in the Asia-Pacific Region and other foreign markets	
Not allowed to engage in any income-generating activities in the Philippines.	Do not earn or derive income in the Philippines. An ROHQ is allowed to derive income in the Philippines

Qualifying Services

Pertains to general administration and planning; business planning and coordination; sourcing and procurement of raw materials and components; corporate finance advisory services; marketing control and sales promotion; training and personnel management; logistic services; research and development services and product development; technical support and maintenance; data processing and communications; and business development.

Income Tax on Regional Headquarters

RAHQ	ROHQ
Shall not be subject to income tax	Shall pay regular corporate income tax or MCIT, whichever is higher

vi. Offshore Bank Units

A branch, subsidiary or affiliate of a foreign banking corporation which is duly authorized by the BSP of the Philippines to transact offshore banking business in the Philippines. (*Section 1(b), PD NO. 1034*)

"Offshore Banking" shall refer to the conduct of banking transactions in foreign currencies

involving the receipt of funds from external sources and the utilization of such funds. (*Id*)

OBUs shall now be taxed as a regular RFC upon the effectivity of the CREATE Act.

Accordingly, OBUs are subject to 25% regular corporate income tax based on their taxable income. (*RR No. 5-2021*)

vii. Special Non-Resident Foreign Corporations

The following NFRCs are subject to a special tax rate:

NRFC	Special Tax Rate
Cinematographic film owner, lessor, or distributor	25%
Lessor of aircraft, machineries, and other equipment	7.5%
Owner or lessor of vessels are chartered by Filipino nationals	4.5%

b. INCOME

i. Definition

An income is the return in money from one's business, labor, or capital invested; gains, profit or private revenue. (*Black's Law Dictionary*)

Income means all wealth that flows into the taxpayer other than as a mere return of capital. It includes the forms of income specifically described as gains and profits including gains derived from the sale or other disposition of capital assets. (*RR No. 02-40, Income Tax Regulation*)

Income was defined as cash received or its equivalent; it is the amount of money coming to a person within a specific time; something distinct from principal or capital. For while capital is a fund, income is a flow. As used in our income tax law, "income" refers to the flow of wealth. (*CIR vs British Overseas Airways*)

ARELLANO UNIVERSITY SCHOOL OF LAW BAR OPERATIONS COMMISSION 2025

Corporation, G.R. Nos. 65773-74, April 30, 1987)

Income may be defined as an amount of money coming to a person or corporation within a specified time, whether as payment for services, interest or profit from investment. Unless otherwise specified, it means cash or its equivalent. Income can also be thought of as a flow of the fruits of one's labor. (*Association of Non-Profit Clubs, Inc. vs. BIR, G.R. No. 228539 dated June 26, 2019; Commissioner of Internal Revenue vs. Shinko Electric Industries Co., Ltd, G.R. No. 226287, July 6, 2021*)

Distinguish Income from Capital

Capital	Income
"fund" or "wealth"	flow of services rendered by capital" or the "service of wealth"
fund	flow
fund of property existing at an instant of time	flow of services rendered by that capital by the payment of money from it or any other benefit rendered by a fund of capital in relation to such fund through a period of time
Wealth	Service of wealth

(*Association of Non-Profit Clubs, Inc. vs. BIR, GR No. 228539 dated June 26, 2019*)

The essential difference between capital and income is that capital is a fund; income is a flow. A fund of property existing at an instant of time is called capital. A flow of services rendered by that capital by the payment of money from it or any other benefit rendered by a fund of capital in relation to such fund through a period of time is called an income. Capital is wealth, while income is the service of wealth. (*Madrigal vs. Rafferty, G.R. No. L-12287, August 7, 1918*)

Distinguish Income from Gross Receipts/Sales

Income	Gross Receipts/Sales
Narrower in scope	Broader in scope
Limited only to gain derived from labor, capital or property, excluding non-income items such as the capital invested, cost of goods sold or those excluded by law from income taxation.	Includes receipts which may constitute capital as well as income.

Distinguish Income from Revenue

Income	Revenue
Private persons or corporations	Government
	All funds or income derived by the government whether from tax or other sources.

(*Ingles, Basic Approach to Income Taxation, 2021 Edition, p. 6*)

ii. Realization and Recognition of Income

a. Existence of Income

There must be gain or profit whether in cash or its equivalent. Income tax applies only when there is income, gain or profit.

Case law provides that in order to constitute "income," there must be realized "gain." Clearly, because of the nature of membership fees and assessment dues as funds inherently dedicated for the maintenance, preservation, and upkeep of the clubs' general operations and facilities, nothing is to be gained from their collection. (*Association of Non – Profit Clubs (ANPC) vs. CIR, G.R. No. 228539, June 26, 2019*)

b. Realization of Income

The gain must be realized or received

ARELLANO UNIVERSITY SCHOOL OF LAW BAR OPERATIONS COMMISSION 2025

Under the realization principle, revenue is generally recognized when both of the following conditions are met:

1. The earning is complete or virtually complete; and
2. An exchange has taken place. (*Manila Mandarin Hotels vs. CIR, CTA Case. 5046, March 24, 1997*)

A taxpayer is deemed to have received items of gross income which have been credited to or set apart for him without restriction. On the other hand, appreciation in value of property is not even an accrual of income to a taxpayer prior to the realization of such appreciation through sale or conversion of the property. (*Sec. 38, RR No. 2-40, February 10, 1940*)

Certainly, these increases in the taxpayer's net worth were not taxable increases in net worth, as they were not the result of the receipt by it of unreported or unexplained taxable income, but were shown to be merely the result of the correction of errors in its entries in its books relating to its indebtedness to certain creditors, which had been erroneously overstated or listed as outstanding when they had in fact been duly paid. The Tax Court's action must be affirmed. (*Fernandez vs. Commissioner of Internal Revenue, G.R. No. L-21551 and L-21557, September 30, 1969*)

c. Recognition of Income

Receipt of income for purposes of taxation may be actual or constructive. (*CIR vs. BPI, G.R. No. 147375, June 25, 2006*)

Distinguish Actual from Constructive Receipt of Income

Actual	Constructive Receipt
Actual and physical receipt.	Occurs when money or its equivalent is placed at the control of the person who rendered the service without restriction by the payor

There is, therefore, constructive receipt, when the consideration for the articles sold, exchanged or leased, or the services rendered has already been placed under the control of the person who sold the goods or rendered the services without any restriction by the payor. (*Ericsson Telecommunications, Inc. v. City of Pasig, G.R. No. 176667, November 22, 2007*)

Examples:

1. Deposits in the bank which are made available by the seller of service without any restrictions.
2. Issuance by the payor of a notice to offset any debt or obligation and acceptance thereof by the seller as payment of services rendered.
3. Transfer of amounts retained by the payor for the account of the seller (RR 16-2005, Sec. 4.108 -4)
4. An item of income must be included in gross income if it is credited to the account of or set apart for the taxpayer, or otherwise made available to the taxpayer, although not yet physically received or placed to his actual possession.

The Doctrine of Constructive Receipt is designed to prevent the taxpayer using the cash basis from deferring or postponing the actual receipt of taxable income. Without the rule, the taxpayer can conveniently select the year in which he will report the income. (Dimaampao, Basic Approach to Income Taxation, 2021 Edition, p. 11)

Taxability of Income

Taxable income means the pertinent items of gross income specified in this Code, less the deductions, if any, authorized for such types of income by this Code or other special laws (*Section 31, NIRC, as amended*)

For income to be taxable, the following requisites must exist:

- (1) there must be gain;
- (2) the gain must be realized or received and
- (3) the gain must not be excluded by law or treaty from taxation. (*CREBA vs. Romulo, GR No. 160756 dated March 9, 2010; CIR*)

ARELLANO UNIVERSITY SCHOOL OF LAW BAR OPERATIONS COMMISSION 2025

vs. Shinko Electric Industries Co., Ltd., GR No. 226287 dated July 6, 2021)

Tests in determining whether income is earned for tax purposes:

1. Realization Test

Unless the income is deemed "realized," there is no taxable income.

This principle requires that revenue must be earned before it is recorded. Thus, the amounts received in advance are not treated as revenue of the period in which they are received but as revenue of the future period or periods in which they are earned. These amounts are carried as unearned revenue, that is, liabilities to transfer goods or render services in the future — until the earning process is complete.

2. Economic Benefit Test or Doctrine of Proprietary Interest

The Economic Benefit Theory provides that anything, which benefits a person materially or economically in whatever way, is taxable under the law. (*BIR Ruling No. 123-97*)

As a general rule, in this jurisdiction, mere increase in the value of the property without actual realization, either through sale or other disposition, is not taxable, the only exception being that even without a sale or other disposition, if by reason of appraisal, the cost basis of property is increased and the resultant basis is used as the new tax base for purposes of computing the allowable depreciation expense, the net difference between the original cost basis and new basis due to appraisal is taxable under the economic-benefit principle. (*BIR Ruling No. 029-98*)

3. Severance Test

There is no taxable income until there is a separation from capital of something of exchangeable value, thereby supplying the realization or transmutation which would result in the receipt of income (*Eisner vs. Macomber, 252 U.S., 189*).

4. Doctrine of Proprietary Interest/Substantial Alteration of Interest Test

Treats stock options, shares of stock or other assets transferred by an employer to an employee to secure better services as taxable. (*Dimaampao, Basic Approach to Income Taxation, 2021 Edition, p. 13*)

5. Claim of Right Doctrine

If the taxpayer receives earnings under a claim of right and without restriction as to its disposition, such earnings are considered income. (*Ingles, Tax Made Less Taxing: A Reviewer with Codals and Cases, 2021 Edition, p. 34*)

6. Control Test

The power to dispose of income is the equivalent of ownership of it. The exercise of that power to procure the payment of income to another is the enjoyment, and hence the realization, of the income by him who exercises it. (*Helvering vs. Horst, 311 U.S. 112*)

7. All Events Test

The accrual of income and expense is permitted when the all-events test has been met. This test requires:

- i. Fixing of a right to income or liability to pay; and
- ii. The availability of the reasonable accurate determination of such income or liability.

The all-events test requires the right to income or liability be fixed, and the amount of such income or liability be determined with reasonable accuracy. However, the test does not demand that the amount of income or liability be known absolutely, only that a taxpayer has at his disposal the information necessary to compute the amount with reasonable accuracy. The all-events test is satisfied where computation remains uncertain, if its basis is unchangeable; the test is satisfied where a computation may be unknown, but is not as much as unknowable, within the taxable year. The amount of liability does not have to be determined exactly; it

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must be determined with "reasonable accuracy." Accordingly, the term "reasonable accuracy" implies something less than an exact or completely accurate amount. (*Commissioner of Internal Revenue vs. Isabela Cultural Corporation*, G.R. No. 172231, February 12, 2007)

iii. Income Sources

Gross income means all income derived from whatever source, including (but not limited to) the following items:

1. Compensation for services "in whatever form paid", including, but not limited to fees, salaries, wages, commissions, and similar items;
2. Gross income derived from the conduct of trade or business or the exercise of a profession;
3. Rents;
4. Royalties
5. Annuities;
6. Prizes and winnings;
7. Pensions;
8. Partner's distributive share from the net income of the general professional partnership;
9. Interests;
10. Gains derived from dealings in property; and
11. Dividends

The list enumerated above is NOT exclusive.

The definition of gross income is broad enough to include passive income subject to specific rates or final taxes. However, since these passive incomes are already subjected to different rates and taxed finally at source, they are no longer included in the computation of gross income which determines taxable income. (*CIR vs. Philippines Airlines, Inc.*, G.R. No. 160628, October 9, 2005)

a. Compensation Income

All remunerations for services performed by an employee under an employer – employee relationship, unless specifically excluded by the Code. (*Sec. 2, RR No. 8- 2018*)

The name by which the remuneration for services is designated is immaterial. Thus, salaries and wages; emoluments and honoraria; allowances (e.g. transportation, representation, entertainment and the like); commissions; fees (including director's fees, if the director is, at the same time, an employee of the employer/corporation); taxable bonuses and fringe benefits (except those which are subject to the Fringe Benefits Tax under Sec. 33 of the Tax Code and the allowable "de minimis" benefits); taxable pensions and retirement pay; and other income of a similar nature constitute compensation income (*Sec. 2(a), RR No. 8- 2018*)

Valuation of Compensation

The following are the rules in determining the value of compensation:

- a. If paid in cash, the cash value of the compensation
- b. If services are paid for in a medium other than money, the fair market value of the thing taken in payment
- c. If a corporation transfer to its employees its own stock as remuneration for services rendered by the employee, the amount is the fair market value of the stock at the time the services were rendered. (*RR No. 2-1998*)

Requisites for compensation to be taxable

- a. There must be personal services actually rendered;
- b. There must be payment for such services rendered;
- c. The payment made is reasonable.

Types of Compensation

The following are the types of compensation that an employee may receive:

- a. Regular Compensation;
- b. Supplemental Compensation; and
- c. 13th month pay and other benefits.

i. Regular Compensation

The following are the items of regular compensation:

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1. Basic Pay
2. Holiday Pay
3. Overtime Pay
4. Night Shift Differential pay
5. Hazard Pay

Exempt from Regular Compensation

1. SSS benefits
2. GSIS benefits
3. Social security benefits, retirement gratuities, pensions and other similar benefits received by resident or nonresident citizens of the Philippines or aliens who come to reside permanently in the Philippines from foreign government agencies and other institutions, private or public.
4. Payments of benefits due or to become due to any person residing in the Philippines under the laws of the United States administered by the United States Veterans Administration.
5. Mandatory government contributions
6. Union dues
7. Compensation for services by a citizen/residents for a foreign government or an international organization - only exempted from withholding, but still subject to regular income tax.
8. Compensation for injuries or sickness.
9. Active hazard pay received by Human Resources for Health during COVID-19 pandemic

ii. Supplemental Compensation

The following are the items of supplemental compensation:

1. Living quarters or meals provided by the employer
2. Fixed or variable transportation, representation and other allowances which are received by an employee.

Representation and transportation allowances fixed in amounts and regularly received by the employees as part of their monthly compensation income shall not be treated as

taxable fringe benefits but shall be considered as taxable compensation income.

3. Amounts of "vacation allowances or sick leave credits" which are paid to an employee.

4. Equity-based compensation

- Stock options
- Restricted share awards/ stock units
- Stock appreciation rights (*RR No. 13-2022*)

5. Pensions, retirement and separation pay

6. Tips or gratuities or gratuities paid directly to an employee by a customer of the employer which are not accounted for by the employee are taxable income but not subject to withholding. (*RR No. 2-1998*)

Exempt from Supplemental Compensation

1. Any amount paid, either as advances or reimbursements for travelling, representation and other bonafide ordinary and necessary expenses incurred by the employee in the performance of his duties are not compensation.

This is known as "Necessary for the Business" rule or "Convenience of the Employer" rule

If given in cash, the employee is required to account or liquidate for the foregoing expenses in accordance with the specific requirements of substantiation.

The excess of actual expenses over advances made shall constitute taxable income if such amount is not returned to the employer.

Reasonable amounts of reimbursements or advances for travelling and entertainment expenses which are pre-computed on a daily basis need not be subject to the requirement of substantiation and to withholding.

Representation and transportation allowance (RATA) and Personal Economic Relief Allowance (PERA) granted to public officers

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and employees constitute reimbursement for expenses incurred in the performance of official duties.

2. Retirement Benefits

May be exempt under RA No. 4917 or under RA No. 7641.

For the retirement benefits to be exempt, the following are the requisites:

RA No. 4917	RA No. 7641
Must not less than 50 years of age at the time of retirement	Must be at least 60 years old, but not beyond 65 years old (however, the 65-year-old rule not mandatory)
In the service of the same employer for at least 10 years	Has served his/her employer for at least 5 years
The retiree should not have previously availed of the privilege under the retirement benefit plan of the same or another employer	Has not previously availed of the privilege under a retirement benefit plan of the same or another employer.
The plan must be reasonable and approved by the BIR.	

3. Separation Pay

Any amount received from the employer due to death, sickness or other physical disability or for any cause beyond the control of the said employee, such as retrenchment, redundancy, or cessation of business. (*RR No. 2-1998*)

4. Maternity Benefit

All female workers, regardless of civil status or the legitimacy of her child, shall be granted 105 days maternity leave with full pay. (*RMC No. 105-2019*)

iii. 13th month pay and other benefits

The following constitute 13th month pay and other benefits:

1. 13th month pay equivalent to the mandatory 1-month basic salary and

2. Other benefits such as Christmas bonus, productivity incentive bonus, loyalty award, gifts in cash or in kind and other benefits of similar nature actually received.

Specifically, the following are included:

- 13th month pay
- 14th, 15th, 16th, and so on, month pay
- Christmas bonus (Yuletide bonus)
- Midyear bonus / Quarterly bonus
- Productivity bonus
- Cash gifts
- Gifts in kind
- Loyalty awards
- Additional Compensation Allowance (ACA) of government employees

The BIR ruled that "love gifts" received by pastors from their pastoral ministry are considered taxable compensation income inasmuch as every form of compensation for personal services is taxable, regardless of how it is earned, by whom it is paid, the label by which it is designated, the basis upon which it is determined, or the form by which it is received. (*BIR Ruling No. DA-214-06, April 5, 2006*)

Tax Treatment of 13th month pay and other benefit

13th month pay and other benefits not exceeding P90,000 are **exempt from income tax**.

Amounts in excess of P90,000 in a calendar year **are subject to regular income tax**

ARELLANO UNIVERSITY SCHOOL OF LAW BAR OPERATIONS COMMISSION 2025

regardless of the kind of employee (i.e., rank-and-file, supervisory, or managerial)

De Minimis Benefits

De minimis benefits are facilities or privileges of relatively small value furnished by the employer merely as means of promoting the health, goodwill, contentment, or efficiency of employees.

However, not all facilities or privileges of relatively small value are considered as de minimis benefits. The BIR provides a specific enumeration of what constitutes de minimis benefits and their specific limitations:

1. Uniform and clothing allowance not exceeding **P7,000 per annum**;

Prior to 2025, the threshold is P6,000. (*RR No. 4-2025*)

2. Employees achievement awards, e.g., for length of service or safety achievement, **in any form, whether in cash, gift certificate, or any tangible personal property**, with an annual monetary value not exceeding P10,000 received by the employee under an established written plan which does not discriminate in favor of highly paid employees;

Prior to 2025, these awards must be in the form of a tangible personal property other than cash or gift certificate. (*RR No. 4-2025*)

3. Daily meal allowance for overtime work and night/ graveyard shift not exceeding 25% of the basic minimum wage on a per region basis;

4. Rice subsidy of P2,000 or one (1) sack of 50 kg, rice per month amounting to not more than P2,000;

5. Laundry allowance not exceeding P300 per month;

6. Gifts given during Christmas and major anniversary celebrations not exceeding P5,000 per employee per annum;

7. Monetized unused leave credits

i. Monetized unused vacation leave credits of private employees not exceeding ten (10) days during the year;

ii. Monetized value of vacation and sick leave credits paid to government officials and employees;

8. Benefits received by an employee by virtue of a collective bargaining agreement (CBA) and productivity incentive schemes, provided that the total annual monetary value received from both CBA and productivity incentive schemes combined do not exceed P10,000 per employee per taxable year;

9. Medical benefits

i. Medical cash allowance to dependents of employees not exceeding P1,500 per employee per semester or P250 per month;

ii. Actual medical assistance, e.g., medical allowance to cover medical and healthcare needs, annual medical/executive check-up, maternity assistance, and routine consultations, not exceeding P10,000 per annum. (*RR No. 2-1998; RMC No. 50-2018*)

All other benefits given by employers which are not included in the above enumeration shall not be considered as de minimis benefits, and hence, shall be subject to income tax as well as withholding tax

Tax Treatment of De Minimis Benefit

If within threshold: Exempt

If above threshold: Excess will form part of 13th month pay and other benefits.

Exception: Benefits from CBA where the entire amount will form part of 13th month pay and other benefits

If 13th month pay and other benefits did not exceed P90,000: Exempt

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If 13th month pay and other benefits exceeded P90,000: Taxable - Regular income tax or the withholding tax on compensation (RIT/WTC), regardless of employee classification

Taxability of Minimum Wage Earners (MWEs)

Compensation income including overtime pay, holiday pay, night shift differential pay, and hazard pay, earned by MWEs who have no other returnable income are NOT taxable and not subject to withholding tax on wages (RA 9504).

Exception: If he receives/earns additional compensation such as commissions, honoraria, fringe benefits, benefits in excess of the allowable statutory amount of P90,000 (RA 10963), taxable allowance, and other taxable income other than the statutory minimum wage (SMW), holiday pay, overtime pay, hazard pay and night shift differential pay.

Any privilege such as meals, living quarters, and other facilities, furnished to an employee for the convenience of the employer, and which is incidental to the requirement of the employee's work or position, the value of that privilege need not be included as compensation. (*Henderson vs. Collector, GR No. L-12954, 1961*)

Fringe Benefits

Fringe benefit means any goods, services, or other benefit furnished or granted in cash or in kind, in addition to basic salaries, to an individual employee, except a rank and file employee. (*Section 33(B), NIRC*)

Fringe benefit means includes but not limited to the following:

- Housing
- Expense Account
- Vehicle of any kind
- Household personnel, such as maid, driver and others

- Interest on loan at less than market rate to the extent of the difference between the market rate and actual rate granted
- Membership fees, dues and other expenses borne by the employer for the employee in social and athletic clubs and similar organizations
- Holiday and vacation expenses
- Expenses for foreign travel
- Educational assistance to the employee or his dependents; and
- Life or health insurance and other non-life insurance premiums or similar amounts in excess of what the law allows. (*Sec. 33(B), NIRC, as amended*)

Computation of FBT

Steps	Computation
Step 1: Value of the Fringe Benefit	Amount of cash paid, expenses shouldered, or depreciation of the property being used by the employee
Step 2: Monetary Value	Value is multiplied by 100% or 50%. The 50% multiplier is usually used when ownership will not transfer to the employee and the employee is only allowed temporary use of property.
Step 3: Grossed-up Monetary Value	This is obtained by dividing the monetary value by: a. 65% if the recipient of the fringe benefit is a managerial and supervisory employees

ARELLANO UNIVERSITY SCHOOL OF LAW BAR OPERATIONS COMMISSION 2025

Steps	Computation
	b. 75% if the recipient of the fringe benefit is a NRANETB managerial and supervisory employees
Step 4: Fringe benefit tax due	The Grossed-up Monetary Value is multiplied by the FBT rate. The FBT rate is 35% as a general rule, but is 25% for NRANETB managerial and supervisory employees.

Exemption from Fringe Benefit Tax

1. Exempt Housing

(a) Housing unit which is situated inside or adjacent to the premises of a business or factory

Adjacent: located within 50 meters from the perimeter of the business premises.

(b) Temporary housing: stay is for three months or less.

2. Exempt Expense Account

Duly receipted for and in the name of the employer.

Expenditures do not partake the nature of a personal expense attributable to the employee.

3. Exempt vehicle - The use of aircraft (including helicopters) owned and maintained by the employer shall be treated as business use.

4. Exempt membership fees - Such expenses may be representation expenses.

To prove, the taxpayer should maintain receipts that indicate the (a) amount, (b) date and place, (c) purpose, (d) professional or business relationship, and (e) name of person and company entertained with contact details.

5. Exempt foreign travel - Business expenses for attending business meetings or conventions. The exemption includes:

(a) Inland travel expenses (such as expenses for food, beverages and local transportation) except lodging cost in a hotel) amounting to an average of USD 300.00 or less per day

(b) The cost of economy and business class airplane ticket.

(c) 70% of the cost of first-class airplane ticket. (30% is subject to FBT)

The expenses should be supported by documents proving the actual occurrences of the meetings or conventions.

6. Exempt educational assistance

(a) Scholarship grant to the employee if:

- I. the education or study involved is directly connected with the employer's trade, business or profession
- II. there is a written contract between them that the employee is under obligation to remain with the employer for a period of time.

(b) Extended by an employer to the dependents of an employee - Exempt if the assistance was provided through a competitive scheme under the scholarship program of the company.

7. Exempt insurance

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(a) Contributions of the employer for the benefit of the employee, pursuant to the provisions of existing law, such as SSS Law or under the GSIS, or similar contributions arising from the provisions of any other existing law.

(b) The cost of premiums borne by the employer for the group insurance of his employees.

(c) Contributions of the employer for the benefit of the employee to retirement, insurance and hospitalization benefit plans. *(RR No. 3-1998)*

Substituted Filing for Employees

Individual taxpayers receiving purely compensation income from only one (1) employer in the Philippines for the calendar year, the income tax of which has been withheld correctly by the said employer, shall not be required to file an annual income tax return (AITR). *(RR No. 2-1998)*

In lieu of the AITR, the Certified List of Employees Qualified for Substituted Filing of ITR filed by the employer with the BIR and stamped "Received" shall be tantamount to the substituted filing of ITRs by employees. *(RR No. 11-2018)*

Not Qualified for Substituting Filing

1. Those deriving compensation from two or more employers concurrently or successively at any time during the taxable year.

2. Those deriving compensation income, the income tax of which has not been withheld correctly resulting to collectible or refundable return.

3. Those deriving other non-business, non-professional-related income in addition to compensation income not subject to final tax.

4. Those whose spouse is disqualified. *(Id.)*

b. Professional Income

A professional is a person formally certified by a professional body belonging to a specific

profession by virtue of having completed a required examination or course of studies and/or practice, whose competence can usually be measured against an established set of standards. It also refers to a person who engages in some art or sport for money, as a means of livelihood, rather than as a hobby. It includes but is not limited to doctors, lawyers, engineers, architects, CPAs, professional entertainers, artists, professional athletes, directors, producers, insurance agents, insurance adjusters, management and technical consultants, bookkeeping agents, and other recipients of professional, promotional and talent fees. *(RR No. 08-2018)*

It is income derived purely from the practice of profession and not under an employer-employee relationship. *(Id.)*

Distinguish Compensation Income from Professional Income

Compensation Income	Professional Income
Fees or remuneration under employer-employee relationship	Fees or remuneration without employer – employee relationship

c. Income from Business

1. Active vs Passive Income

Distinguish Active from Passive Income

Active Income	Passive Income
Earned in Active Pursuit and performance of business. <i>(RMC No. 50-2018)</i>	Not earned in the active pursuit and performance of business, but earned from the taxpayer's assets.
In general, it is subject to regular income tax	In general, subject to specific rates or final rates.

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(Iconic Beverages, Inc. vs CIR, CTA Case No. 8607 [Resolution], January 6, 2016)

Final Withholding Tax

Final withholding tax is a kind of withholding tax which is prescribed on certain income payments and is not creditable against the income tax due of the payee on other income subject to regular rates of tax for the taxable year. The income tax withheld constitutes the full and final payment of the income tax due on the particular income subjected to final withholding tax. In general, passive incomes under the NIRC are subject to final withholding tax. (*RR No. 2-1998*)

a. FWT on Individuals

The following are the items of income subject to final income tax:

i. Dividend

Dividend income from domestic corporations is subject to final income tax.

This includes:

- i. Dividends actually or constructively received from a domestic corporation
- ii. Share of an individual in the distributable net income after tax of a partnership (not including a GPP)
- iii. Share in the net income after tax of an association, joint account, or a joint venture (not including exempt joint ventures)

Individual	FWT
RC, NRC, RA	10%
NRAETB	20%
NRANETB	25%

Dividend income from foreign corporations are subject to regular income tax, especially for resident citizens who are taxed on their income derived from sources outside the Philippines.

ii. Royalties

The following are the final income tax for royalties:

Sources	FWT
Literary compositions, books, musical compositions	10%
Other royalties	20%

iii. Interest Income

a. Interest from currency bank deposits

General rate: 20% FWT

Exempted: Long term deposit

Requisites for exemption of interest income from long term currency bank deposit:

1. Depositor is an individual RC, NRC, RA, or NRAETB
2. Must be under the name of the individual
3. Must be in denominations of P10,000
4. Must be received / issued by banks only and not by other financial institutions
5. Must be executed in the form of savings, common or individual trust funds, deposit substitutes, investment management accounts and other investments evidenced by certificates in such form prescribed by the Bangko Sentral ng Pilipinas (BSP)
6. Must have a maturity period of five (5) years
7. Must not be terminated by the investor before the 5th year

NOTE: Should the holder pre-terminate the deposit before the 5th year, a final tax on the entire income shall be withheld by the bank based on the remaining maturity thereof:

Year	FWT
4 years to less than 5 years	5%
3 years to less than 4 years	12%

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Less than 3 years	20%
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condition to receiving the prize or award.

b. Yield or any monetary benefit from deposit substitutes and interest income from government securities

The term "public means borrowing from 20 or more Individual or corporate lenders at any one time. The mere flotation of a debt instrument is not deemed a "deposit substitute" If there are only not more than 19 individual or corporate lenders at any one time.

Government securities need not comply with the 19-lender rule.

General rate: 20% FWT (*Section 22 (Y), NIRC, as amended; RR No. 14-2012*)

c. Interest Income under expanded foreign currency deposit

Individual	FWT
Resident	15%
Non-resident	Exempt

iv. Prizes and Winnings

The following are the rates for prizes and winnings:

Prizes	Winnings
General Rate: 20%	General Rate: 20%
Regular Income Tax: If less than P10,000	20% FWT: If less than P10,000
	PCSO winnings: Exempted

The following are exempt prizes:

i. Prizes and awards made primarily in recognition of charitable, civic, literary, educational, artistic, religious, and scientific achievement.

Conditions:

- The recipient was selected without any action on his part to enter the contest or proceeding; and The recipient is not required to render substantial future services as a

ii. All prizes and awards granted to athletes in local and international sports competitions and tournaments and sanctioned by their national sports associations. (*Section 32, NIRC, as amended*)

National sports association are those duly accredited by the Philippine Olympic Committee. (*RA No. 7549*)

v. Tax Informer's Reward

Information shall not refer to a case already pending or previously investigated by the BIR.

Subjected to 10% FWT of the amount received or P1,000,000 per case, whichever is lower. (*Section 282(A), NIRC, as amended*)

The following are disqualified from being a tax informer:

- a. BIR official/ employee
- b. Any other incumbent public official or employee;
- c. Relative within the 6th degree of consanguinity of A and B
- d. Though already retired or separated from service, A and B who acquired the information in the course of the performance of their duties during their incumbency. (*RR 16-2010*)

Cash rewards of informers shall be subject to 10% FWT. (*Section 282(B), NIRC, as amended*)

b. Final tax on Corporation

The following items of income subject to final tax:

i. Dividend

Dividend income includes:

- a. Intercompany dividends/ Dividend received by a domestic corporation

From a Domestic Corporation

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It shall not be subject to income tax. (*Section 27(D), NIRC, as amended by CREATE*)

From a Foreign Corporation

It shall be subjected to regular corporate income tax

Exceptions:

It shall be exempted if compliant with conditions:

1. **Reinvestment Test:** Reinvestment of dividends to the domestic corporation's operations in the Philippines

In order to be exempt, the dividends actually received or remitted into the Philippines should be reinvested in the business operations of the domestic corporation in the Philippines within the next taxable year from the time the foreign-sourced dividends were received.

Reinvestment shall be limited to funding the:

- i. working capital requirements
- ii. capital expenditures
- iii. dividend payments
- iv. investment in domestic subsidiaries
- v. infrastructure project

2. **Significant Test:** Domestic corporation holds directly at least 20% of the outstanding voting stock of the foreign corporation.

3. **Holding Period Test:** Shareholdings have been held for a minimum of two years at the time of dividend distribution

The 2-year period is uninterrupted. In case the foreign corporation has been incorporated for less than two years, the shareholdings must have been held since incorporation. (*RR No. 5-2021*)

In case of **partial or non-utilization** of the foreign-sourced dividends, the domestic corporation shall pay the income tax due, plus surcharge, interest and penalties. (*RR No. 5-2023*)

(b) Dividends received by a RFC from a DC shall not be subject to FWT since it is **intercorporate dividends**.

(c) Dividend Received by a NRFC - it shall be subject to 25% FWT.

However, it may be subject to 15% rate under tax sparing rule or apply predominance test.

Tax Sparing Rule

Tax credit against the tax due from the NRFC (taxes deemed to have been paid in the Philippines) shall be the difference between 15% and regular income tax rate. (*Section 28 (B) (5) (b), NIRC, as amended by CREATE*)

Predominance Test

Dividends from a foreign corporation is income from within the Philippines, unless less than 50% of the gross income of such foreign corporation for the three-year period ending with the close of its taxable year preceding the declaration of such dividends or for such part of such period as the corporation has been in existence) was derived from sources within the Philippines; but only in an amount which bears the same ratio to such dividends as the gross income of the corporation for such period derived from sources within the Philippines bears to its gross income from all sources. (*Section 42 (A)(2)(b), NIRC, as amended*)

ii. Royalties

The following are the final income tax for royalties:

Sources	FWT
Literary compositions, books, musical compositions	20%
Other royalties	20%

iii. Interest

a. Interest from currency bank deposits

General rate: 20% FWT

(a) Dividends Received by a RFC

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ARELLANO UNIVERSITY SCHOOL OF LAW BAR OPERATIONS COMMISSION 2025

Exception: Long term deposit shall be subject to regular income tax.

b. Yield or any monetary benefit from deposit substitutes and interest income from government securities

General rate: 20% FWT

c. Interest Income under expanded foreign currency deposit

Corporation	FWT
Domestic and Resident Foreign	15%
Non-resident	Exempt

NOTES:

- i. Prizes of corporations are subject to regular corporate income tax, as they are omitted from the enumeration of those subject to final income tax for corporations.
- ii. Winnings are, generally, not applicable to corporations, Corporations cannot enter into raffle draws or lottery
- iii. Tax Informer's Reward is a type of income that are only applicable to individual.

d. Income from Dealings with Property

1. Capital vs. Ordinary Asset

Definition of Capital Asset

Capital assets shall refer to all real properties held by a taxpayer, whether or not connected with his trade or business, and which are not included among the real properties considered as ordinary assets under Section 39(A)(1) of the NIRC, as amended.

Definition of Ordinary Asset

Ordinary assets shall refer to all real properties specifically excluded from the definition of capital assets under Section 39(A) (1) of the Tax Code, namely:

1. Stock in trade of a taxpayer or other real property of a kind which would properly be included in the inventory of the taxpayer if on hand at the close of the taxable year;

2. Real property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business;

3. Real property used in trade or business (i.e., buildings and/ or improvements) of a character which is subject to the allowance for depreciation provided for under Section 34(F) of the Tax Code; or

4. Real property used in trade or business of the taxpayer.

5. Real properties acquired by banks through foreclosure sales. (*RR No. 7-2003*)

Taxation of Capital Gains

General rule: Capital Gains are subject to regular income tax.

The rules on the computation of gain on sale of ordinary assets shall be similarly observed. However, there are additional rules that are unique to sale of capital assets.

i. Holding Period Rule

In the case of a taxpayer, other than a corporation, only the following percentages of the gain or loss recognized upon the sale or exchange of a capital asset shall be taken into account in computing net capital gain, net capital loss, and net income.

Period	Percentage
Held for not more than twelve (12) months	100%
Held for more than twelve (12) months	50%

ii. Capital Loss Limitation Rule

Applicable for both individuals and corporations.

ARELLANO UNIVERSITY SCHOOL OF LAW BAR OPERATIONS COMMISSION 2025

Losses from sales or exchange capital assets shall be allowed only to the extent of the gains from such sales or exchanges,

If a bank or trust company incorporated under the laws of the Philippines, a substantial part of whose business is the receipt of deposits, sells any bond, debenture, note, or certificate or other evidence of indebtedness issued by any corporation, with interest coupons or in registered form, any loss resulting from such sale shall not be subject to the foregoing limitation and shall not be included in determining the applicability of such limitation to other losses.

iii. Net Capital Loss Carryover

If any taxpayer, other than a corporation, sustains in any taxable year a net capital loss, such loss (in an amount not in excess of the net income for such year) shall be treated in the succeeding taxable year as a loss from the sale or exchange of a capital asset held for not more than twelve (12) months. *(Section 39, NIRC, as amended)*

Exceptions are the following capital asset transactions which are tax differently:

Gains on Dealing in Capital Asset	Tax Rate
Net Capital Gains from sale, barter, exchange, or other disposition of shares of DC not traded in stock exchange.	15% on net capital gain. <i>(Section 24, NIRC, as amended)</i>
Sale, barter, exchange, or other disposition of shares of DC traded in stock exchange.	Stock transaction tax of 0.60% of Gross Selling Price or gross value in money of shares of stock. <i>(Section 127 (A), NIRC, as amended)</i>

Gains on Dealing in Capital Asset	Tax Rate
Sale, exchange, or other disposition of real property situated in the Philippines and classified as capital asset	6% on capital gains based on the higher between: (a) gross selling price; and (b) fair market value of the property. <i>(Section 24(D), NIRC, as amended)</i>

Transaction not subject to 6% capital gains tax:

i. Sale to the government, its political subdivisions, instrumentalities or GOCC. - The individual taxpayer has option to either:

- (a) pay the 6% CGT; or
- (b) subject the income from sale to the graduated income tax rates.

ii. Sale of principal residence provided the following conditions are satisfied:

- (a) The proceeds from sale of the principal residence are fully utilized to acquire/construct a new principal residence within 18 months from the sale of old principal residence.
- (b) The BIR is notified of the intention to avail tax exemption within 30 days from sale of the principal residence.
- (c) The 6% CGT is deposited in an escrow account.
- (d) Tax exemption is availed once every 10 years only.

In case there is no full utilization of the proceeds from sale, the portion of the gain proportionate to the unutilized proceeds from sale will be subject to CGT.

ARELLANO UNIVERSITY SCHOOL OF LAW BAR OPERATIONS COMMISSION 2025

e. Situs of Income Taxation

The following items of gross income shall be treated as gross income from sources within the Philippines:

Income	Test of Source
Interest	Debtor's Residence
Income from services	Place or performance of the services rendered. If a service-based company operates in various countries and providing services to clients, then the income earned is allocated to the countries where the services are performed, taking into accounts factors such as the time spent, resources utilized, or value created in each jurisdiction. (RMC No. 5-2024)
Rental and Royalties	Location of the property or place where the intangible is used.
Gain on sale of real property	Location of Property.
Gain on sale of personal property (except sale of shares of a domestic corporation)	Place of sale
Gain from the sale of shares of stock in a domestic corporation	Treated as derived entirely from sources within the Philippines, regardless of where the shares are sold.

Income	Test of Source
Dividends from domestic corporation	Presumed to be income within the Philippines
Dividends from foreign corporation	Predominance Test

Income Partly within and without:

Income covered:

- i. Services rendered partly within and without the Philippines
- ii. Sale of personal property produced (wholly or partly) within and sold without Philippines
- iii. Sale of personal property produced (wholly or partly) within and sold within Philippines

The Supreme Court ruled that turnkey contracts were actually divisible contracts which each had different stages, with each stage having different tax implication:

- i. For the stage involving design, engineering, and procurement of equipment and supplies, these were considered outside the hands of the Philippine taxing authority as these were all done in Japan
- ii. For the stages involving the actual installation and construction, these were all considered within the jurisdiction of the Philippine taxing authority as the construction and installations were all done in the Philippines. (CIR vs. Marubenj, G.R. No.137377, December 18, 2001)

f. Gross Income vs Net Income vs Taxable Income

Gross Income

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All income derived from whatever source, including (but not limited to) the following items:

1. Compensation for services in whatever form paid, including, but not limited to fees, salaries, wages, commissions, and similar items;
2. Gross income derived from the conduct of Trade of business or the exercise of a profession;
3. Rents;
4. Royalties;
5. Annuities;
6. Prizes and winnings;
7. Pensions;
8. Partner's distributive share from the net income of the general professional partnership;
9. Interests;
10. Dividends; and
11. Gains derived from Dealings in property (*Sec. 32[A], NIRC, as amended*)

The definition of gross income is broad enough to include passive income subject to specific rates or final taxes. However, since these passive incomes are already subjected to different rates and taxed finally at source, they are no longer included in the computation of gross income which determines taxable income. (*CIR vs. Philippines Airlines, Inc., G.R. No. 160628, October 9, 2005*)

Income from Whatever Source Derived

Gross Income in its broad sense, means, all income from whatever source, derived within or without the Philippines, legal or illegal. The NIRC doesn't distinguish between legal and illegal income. (*Section 32, NIRC, as amended*)

Hence, proceeds from embezzlement or swindling, for instance, are income because the income recipient has already complete dominion over them and can use such for his economic benefit. If a taxpayer receives income, legally or illegally, without consensual recognition of obligation to repay, that income is taxable. (*James vs US, 366 U.S. 213, 1961*)

While it has been held that the phrase "from whatever source derived" indicates a legislative policy to include all income not expressly exempted within the class of taxable income under our laws, the term "income" has been variously interpreted to mean "cash received or its equivalent," "the amount of money coming to a person within a specific time" or "something distinct from principal or capital." Otherwise stated, there must be proof of the actual or, at the very least, probable receipt or realization by the controlled taxpayer of the item of gross income sought to be distributed, apportioned, or allocated by the CIR. (*CIR vs Filinvest Development Corporation, GR Nos. 163653 & 167689, July 19, 2011*)

Distinguish Gross Income vs Net Income vs. Taxable Income

Gross Income	Net Income	Taxable Income
Income from whatever source, including, but not limited to those enumerated in Section 32(A) of NIRC.	Gross income less statutory deductions (<i>RR No. 02-04</i>)	Pertinent items of gross income specified in the NIRC less any deduction, if any, authorized for such types of income by this Code or another law (<i>Sec. 31, NIRC</i>)
It does not include income excluded by law, or which are exempt from income		

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tax. (Sec. 32 (B), NIRC, as amended)		
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For Individuals:

Taxable Income is equal to net income. **No more deduction for exemptions** (personal, additional and premium for health insurance) as it has been **repealed by TRAIN Law**.

For Corporations:

Taxable income is equal to net income.

Gross Sales/Revenue/Receipts	Xxx
Add Other income	Xxx
Less: Cost of Sales or Cost of Services	Xxx
Total Gross Income	Xxx
Less: Allowable Deductions (Itemized or Optional Standard Deductions)	Xxx
Taxable Income	Xxx

Inclusions and Exclusion from Gross Income

i. Rent

Inclusion Subject to Regular Income Tax	Final tax	Exclusion
Rent (including advance rent)	Rent income by NFRC and/or NРАНETB	
Obligation of lessor assumed by the lessees		Obligation of lessor not assumed by the lessees
Leasehold improvements going to the lessor		Leasehold improvements going to the lessee

Inclusion Subject to Regular Income Tax	Final tax	Exclusion
Forfeited or Applied security deposit		Security deposit

ii. Insurance Proceed

Inclusion Subject to Regular Income Tax	Exclusion
Interest on insurance proceeds (RR No. 2-1940)	Life insurance proceeds (Section 34(B)(1), NIRC, as amended)
Annuities or proceeds in excess of premiums (Id.)	Return of premiums (Section 34(B)(2), NIRC, as amended)
Proceeds of crop insurance (Id.)	Health and accident insurance (RR No. 2-1940)
Excess of proceeds over cost of acquired insurance	Property Insurance

iii. Prizes

Inclusion Subject to Regular Income Tax	Final tax	Exclusion
Prizes not less than P10,000 for individual	Prizes in excess of P10,000	Prizes in connection to recognition of charitable, civic, literary, educational, artistic, religious, and scientific achievement. Subject to conditions:

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Inclusion Subject to Regular Income Tax	Final tax	Exclusion
		<p>1. The recipient was selected without any actions on his part to enter the contest or proceeding, and</p> <p>2. The recipient is not required to render substantial future services as a condition to receiving the prize or award.</p>
Prizes for corporation	Prizes for NRANETB and NFRC which subject to 25% FWT	Prizes of athletes, whether local or international sport competition or tournament, sanctioned by their national sport association (i.e., Philippine Olympic Committee)
Foreign Prizes for RC, DC		

iv. Winnings

Inclusion Subject to Regular Income Tax	Final tax	Exclusion
Winnings, corporation	Winnings, individual (20%)	Winnings from PCSO with not less than P10,000
Foreign Prizes for RC, DC	Winnings from PCSO with more than P10,000 (20%)	
	Winnings, NRANETB (25%)	

v. Dividend Income

Inclusion Subject to Regular Income Tax	Final tax	Exclusion
Dividend from foreign corporation	Dividend from DC	Intercompany dividends
Share in the net income of GPP	Share in the net income of commercial partnership	Dividend from FC to DC provided that it is compliant with (1) Reinvestment Test; (2) Significance Test; (3) Holding Period Test
Share in the net income of exempt joint ventures	Share in the net income of taxable joint ventures	

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Inclusion Subject to Regular Income Tax	Final tax	Exclusion
Share in the net income of co-ownerships	Share in the net income of co-ownerships which undivided for 10 years	Dividends paid by real estate investment trust (<i>RA No. 9856</i>)
	Stock dividend if it gives the shareholder an interest different form that which his former stock holdings represented	Stock dividends
Liquidating dividends in excess of cost		Liquidating dividends

vi. Interest Income

Inclusion Subject to Regular Income Tax	Final tax	Exclusion
Long term deposits of DC and RFC	Currency bank deposits (20%)	Long term deposits of individuals
Interest on insurance proceeds	Yield from deposit substitute and interest income on Government securities (20%)	Interest on CARP
Interest, in general	Interest from expanded foreign currency deposit system (15%)	Interest from EFCDS of non-resident

Inclusion Subject to Regular Income Tax	Final tax	Exclusion
Foreign interest of RC and DC		Investment income from registered retirement plans.

vii. Tax Refunds

Inclusion Subject to Regular Income Tax	Exclusion
Documentary Stamp Tax	Philippine Income Tax
Excise Tax	Donor's Tax
FBT	Estate Tax
Percentage Tax	Stock transaction Tax
Local taxes	VAT
Foreign income tax claimed as allowable deductions	Foreign income tax claimed as tax credits

viii. Forgiveness of Debt

Inclusion Subject to Regular Income Tax	Final tax	Exclusion
Debtor rendered services	Forgiveness of shareholder debt by Corporation. The transaction has the effect of the payment of a dividend. (<i>RR No. 2-1940</i>)	No services rendered

ix. Recovery of Bad Debts

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Inclusion Subject to Regular Income Tax	Exclusion
Writeoff reduced taxable income.	Writeoff did not reduce taxable income.

Tax Benefit Rule

The recovery of bad debts previously allowed as deduction in the preceding year/s shall be included as part of gross income in the year of such recovery to the extent of the income tax benefit of said deduction. (RR No. 5-1999)

x. Damage Recovery

Inclusion Subject to Regular Income Tax	Exclusion
Actual damages on recovery of profits and loss of earning capacity	Actual damages of loss of capital and property damage
	Moral, Exemplary, Nominal and Temperate Damage

xi. Other Income Items

Inclusion Subject to Regular Income Tax	Final tax	Exclusion
Wagering/Gambling gains	Informer's reward	Income by foreign government
Illegal Income		Income exempt by treaty or international agreements
Income from theft and hidden treasures		Gift received by done and Bequest and devises received in succession.

Distinguish Exclusion from Deductions

Exclusion	Deductions
Flow of wealth (Income) to the taxpayer which is not treated as part of gross income due to its exemption by law or does not come within the definition of income	Amounts which the law allows to be subtracted from gross income in order to arrive at the net income
Pertains to the computation of GROSS INCOME	Pertains to the computation of TAXABLE INCOME
Something received or earned by the taxpayer but do not form part of gross income	Something spent or paid in earning gross income (i.e. expenses)

1. Tax Deductions vs. Tax Credits

Distinguish Tax deductions from Tax Credits

Tax Deductions	Tax Credits
It refers to the allowed reductions against gross income for tax purposes.	It refers to an amount that is subtracted directly from one's total tax liability. It is an allowance against the tax itself or a deduction from what is owed by a taxpayer to the government.
It reduces the income that is subject to tax in order to arrive at taxable income.	It reduces the tax due, including - whenever applicable - the income tax that is determined after applying the corresponding tax rates to taxable income.

(Banco De Oro vs. Republic, G.R. No. 198756, January 13, 2015)

Types of deductions:

1. Itemized deductions – deductions that are claimed per item:

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- i. Ordinary allowable deductions
- ii. Special allowable deductions
2. Optional Standard Deductions (40%) under Sec. 34(L)

Itemized Deductions

These are all the ordinary and necessary expenses paid or incurred during the taxable year in carrying on or which are directly attributable to the development, management, operation and/or conduct of the trade, business or exercise of a profession, including a reasonable allowance for salaries, travel, rental, and entertainment expenses. (*RMC No. 40-2011*)

Requisites for the deductibility of ordinary and necessary trade, business, or professional expenses

1. Expense must be ordinary and necessary;
2. Must have been paid or incurred during the taxable year;
3. Must have been paid or incurred in carrying on the trade or business of the taxpayer; and
4. Must be supported by receipts, records, or other pertinent papers (*CIR vs Isabela Cultural Corporation, G.R. No. 172231, February 12, 2007*)

When expenses can be considered as ordinary and necessary to the taxpayer

An expense will be considered "necessary" where the expenditure is appropriate and helpful in the development of the taxpayer's business. It is "ordinary" when it connotes a payment which is normal in relation to the business of the taxpayer and the surrounding circumstances. (*Atlas Consolidated Mining and Development Corporation vs CIR, G.R. No. L-26924, January 27, 1981*)

Non-deductibility of Illegal Expenses

Any payment made, directly or indirectly, to an official or employee of the national government, or to an official or employee of any local government unit, or to an official or employee of a government-owned or controlled corporation, or to an official or employee or representative of a foreign

government, or to a private corporation, general professional partnership, or a similar entity, if the payment constitutes a bribe or kickback shall be disallowed as deductions. (*Section 34(A)(c), NIRC, as amended*)

Other expenses that may be allowed as deductions for income tax purposes

Subject to the qualifications laid down in Section 34 of the NIRC, as amended, the following may be allowed as deductions for income tax purposes:

1. Interest
2. Taxes
3. Losses
4. Bad debts
5. Depreciation
6. Depletion of Oil and Gas Wells and Mines
7. Charitable and Other Contributions
8. Research and Development
9. Pension Trusts

Items not considered as non-deductible

In general, no deduction shall in any case be allowed in respect to the following:

1. Personal, living or family expenses;
2. Any amount paid out for new buildings or for permanent improvements, or betterments made to increase the value of any property or estate;
3. Any amount expended in restoring property or in making good the exhaustion thereof for which an allowance is or has been made; or
4. Premiums paid on any life insurance policy covering the life of any officer or employee, or of any person financially interested in any trade or business carried on by the taxpayer, individual or corporation, when the taxpayer is directly or indirectly a beneficiary under such policy.

In respect of losses from sales or exchanges, no deductions shall be allowed in any case if the sale or exchange is directly or indirectly:

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1. Between members of a family. For purposes of this paragraph, the family of an individual shall include only his brothers and sisters (whether by the whole or half-blood), spouse, ancestors, and lineal descendants; or

2. Except in the case of distributions in liquidation, between an individual and corporation more than fifty percent (50%) in value of the outstanding stock of which is owned, directly or indirectly, by or for such individual; or

3. Except in the case of distributions in liquidation, between two corporations more than fifty percent (50%) in value of the outstanding stock of which is owned, directly or indirectly, by or for the same individual if either one of such corporations, with respect to the taxable year of the corporation preceding the date of the sale of exchange was under the law applicable to such taxable year, a personal holding company or a foreign personal holding company;

4. Between the grantor and a fiduciary of any trust; or

5. Between the fiduciary of a trust and the fiduciary of another trust if the same person is a grantor with respect to each trust;

6. Between a fiduciary of a trust and beneficiary of such trust. (*Section 36, NIRC, as amended*)

2. Optional Standard Deductions

In lieu of the above enumerated allowable deductions (expenses discussed above). Section 34(L) of the NIRC provides for an optional standard deduction (OSD) which is:

i. For Individuals – 40% of Gross Sales/ gross receipts

ii. For Corporations – 40% of Gross Income

It is a fixed percentage deduction without regard to any actual expenditure in lieu of itemized deduction.

Who are allowed to deduct OSD?

i. Individuals

(a) Allowed to all kinds of individual except non – resident alien.

(b) Those who are under the graduated tax table of 0-35%

ii. General professional Partnership or its partners – however, they may avail of it only once.

iii. Domestic/ Resident Corporations – only corporations whose income in whole or in part is not exempt or preferential rate.

General Rules on OSD

i. Unless the taxpayer signifies in his return to elect OSD, he is considered having availed of the itemized deduction.

Such election when made by the qualified taxpayer, is irrevocable for the year in which the election was made; however, he can choose itemized deductions on the succeeding years (*RR No. 16-2008*)

ii. Individuals availing OSD are not allowed to deduct Cost of Sales/Services as the basis of OSD is gross sales/receipts

While for Corporations, they are allowed to deduct the cost of sales/services. (*Section 34(L), NIRC, as amended*)

Rules on OSD on General Professional Partnership

The distributable net income of the partnership may be determined by claiming either itemized deductions or OSD. The share in the net income of the partnership, actually or

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constructively received, shall be reported as taxable income of each partner.

The partners comprising the GPP can no longer claim further deduction from their distributive share in the net income of the GPP and are not allowed to avail of the 8% income tax rate option since their distributive share from the GPP is already net of cost and expenses

If Partnership chooses, **Itemized Deduction**, Partners may claim **Itemized Deductions ONLY**.

If Partnership chooses, **OSD**, Partners may claim Neither itemized or optional.

If the partner also derives other income from trade, business or practice of profession apart and distinct from the share in the net income of the GPP, the deduction that can be claimed from the other income would either be the itemized deductions or OSD.

Distinguish Itemized Deductions from Optional Standard Deduction (OSD)

Itemized Deduction	OSD
As a general rule, itemized deductions are not subject to limitation in the amount that may be allowed as a deduction.	OSD is limited to: 40% of gross sales or gross receipts for individuals; or 40% of gross income for corporations.
Itemized deductions should be substantiated by receipts, records, or other pertinent papers.	Does not require proof of substantiation.
Shall apply by default.	Should be chosen or elected during the filing of the first quarterly income tax return for the year.

g. Withholding Taxes

1. Rationale

Withholding taxes are taxes paid in advance. These are taxes deducted before receipt of cash by the income earner, seller, or transferee.

Importance of Withholding

1. To provide the taxpayer a convenient manner to meet his probable tax liability.
2. To ensure the collection of tax which can otherwise be lost or reduced through failure to file returns
3. To improve the government's cash flow. (*Chamber of Real Estate and Builders' Association, Inc. vs Romulo, G.R. No. 160756*)

Withholding tax is a method of collecting income tax in advance, in the operation of the withholding tax system, the payee is the taxpayer, the person on whom the tax is imposed, while the payor, a separate entity, acts no more than an agent of the government for the collection of the tax in order to ensure its payment. (*LG Electronics Philippines, Inc. vs. Commissioner of Internal Revenue, G.R. No. 165451, December 03, 2014*)

Obligation to Withhold

The obligation to withhold is imposed upon the buyer. payor of income although the burden of tax is really upon the seller-income earner/payee. (*RR No. 11-2018*)

The person deducting is called the **withholding agent**.

Who are exempted from withholding taxes?

The withholding of tax shall not apply to income payment made on the following:

1. National government and its instrumentalities, including provincial, city, and municipal governments and GOCCs;

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2. Persons enjoying exemption from payment of income taxes pursuant to the provisions of any law, general or special, such as but not limited to the following:

(a) Sales of real property by a corporation which is registered with and certified by the Housing and Land Use Regulatory Board (HLURB), or the Housing and Urban Development Coordinating Council (HUDCC), as engaged in socialized housing project where the selling price of the house & lot or only lot, does not exceed the socialized housing price applicable to the area as prescribed and certified by the said council/board;

(b) Corporations which are exempt from the income tax under Sec. 30 of the Tax Code, as amended, and GOCCs exempt from income tax under Sec. 27 (A)(C) of the same code.

However, the income payments arising from any activity which is conducted for profit or income derived from real or personal property shall be subject to withholding tax as prescribed in these regulations;

3. Joint ventures or consortium formed for the purpose of undertaking construction projects, or engaging in petroleum, coal, geothermal, and other energy operations pursuant to an Operating or Consortium Agreement under a service contract with the government;

4. Individuals who earn P250,000.00 and below from a lone income payor upon compliance with these conditions:

(a) Individual has executed a payee's sworn declaration of gross receipts;

(b) Sworn declaration has been submitted to the lone income payor/withholding agent on or before January 15 of each year, or before the initial income payment, whichever is applicable.

Timing of Withholding

The obligation to deduct and withhold the tax arises at the time the income has become

payable. (*Section 58 (C), NIRC, as amended by EOPTA; RR No. 4-2024*)

Prior to the EOPTA, the obligation to withhold arises at the time an income payment is paid or payable, or the income payment is accrued or recorded as an expense or asset, whichever is applicable, in the payor's books, whichever comes first.

2. Creditable vs. Final Withholding Taxes

Definition of Creditable Withholding Tax

Withholding taxes on ordinary business income which is still subjected to income tax and therefore, is deductible as tax credit. (*RR No. 02-98*)

Under the creditable withholding tax system, taxes withheld on certain income payments are intended to equal or at least approximate the tax due of the payee on said income. The income recipient is still required to declare the income payment received as part of the gross income to file an income tax return and/or pay the difference between the tax withheld and the tax due on the income. Taxes withheld on income payments covered by the expanded withholding tax and compensation income are creditable in nature.

A CWT is considered a prepayment or an advance payment of eventual income taxes due at the end of the taxable year. Taxes withheld on certain income payments are intended to equal or at least approximate the tax due of the payee on said income.

The payor endorses the pertinent Certificate of Creditable Tax Withheld at Source to the payee for use by the payee against his tax liability at the end of a taxable year.

NOTE: The claims for tax credit of any creditable income tax deducted and withheld in a previous period can still be creditable in the subsequent calendar or fiscal year, provided that the same had been declared in the tax return where the corresponding income is reported.

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The following are creditable withholding taxes:

- i. Expanded Withholding Tax (EWT) on certain income payments;
- ii. Withholding Tax on Compensation;
- iii. Withholding Tax on money payments to the government

Definition of Final Withholding Tax

Withholding of final tax on certain incomes is a kind of withholding tax which is prescribed on certain income payments, and is not creditable against the income tax due of the payee on other income subject to regular rates of tax for the taxable year.

The liability of payment of tax rates rests primarily on the payor as the withholding agent. Thus, in case of failure to withhold the tax or under-withholding, the deficiency tax shall be collected from the payor/withholding agent. (*RR No. 02-98*)

The amount of income tax withheld by the withholding agent is constituted as a full and final payment of the income tax due from the payee on the said income. The liability for payment of the tax rests primarily on the payor as a withholding agent. Thus, in case of his failure to withhold the tax or in case of under withholding, the deficiency tax shall be collected from the payor/withholding agent.

The payee is not required to file an income tax return for the particular income. Note, however, that individual and corporate taxpayers are still required to declare in the ITR the gross income which have been subjected to final tax.

The finality of the withholding tax is limited only to the payee's income tax liability on the particular income. It does not extend to the payee's other tax liability on said income, e.g., percentage tax.

Distinguish Final Withholding Tax from Creditable Withholding Tax

FWT	CWT
Amount of Tax Collected	
Full and final payment of the income due from the payee on said income	Intended to equal, or at least approximate the tax due, from the said payee on said income
Primarily Liable	
Withholding agent	Taxpayer
Need to File a Return	
Payee NOT Required to file	Income recipient is REQUIRED to file ITR, and/or pay the difference between tax withheld and tax due on income
Coverage	
ALL income subject to final taxes (e.g. Passive income, Gross income of NRA-NETB)	Those income payments covered by EWT (Rev. Regs. 02-98) (e.g. Professional fees, talent fees, income payment to partners in GPP)

3. Duties of Withholding Agent

- i. Filing of quarterly withholding tax returns;
- ii. The submission to the payee, in respect of his or its receipt during the calendar year, of a written statement showing the income or other payments made by the withholding agent during the quarter or year, and the amount of tax deducted and withheld therefrom; and
- iii. Filing with the BIR of the Reconciliation Statement of Quarterly Payment, and a list of payees and income payments.

Consequences of the failure of the withholding agent to collect and remit taxes.

Any person required to withhold, account for, and remit any tax imposed by this code or who willfully fails to withhold such tax, or account

ARELLANO UNIVERSITY SCHOOL OF LAW BAR OPERATIONS COMMISSION 2025

for and remit such tax, or aids or abets in any manner to evade such any tax or the payment thereof, shall, in addition to other penalties provided for under this chapter, be liable upon conviction to a penalty equal to the total amount of tax not withheld, or not accounted for and remitted. (*Section 251, NIRC, as amended*)

Any income tax withheld by the income payor/ withholding agent in excess of what is prescribed shall be refunded to the payee. The income payor/ withholding agent shall reflect the amount refunded as adjustment to the remittable withholding tax due for the 1st quarter withholding tax return. It shall also be reflected in the Alphabetical List of Payees, to be attached in the said 1st quarter return.

Consequences of the failure of the withholding agent to refund excess withholding tax

Any employer/withholding agent who fails or refuses to refund any excess withholding tax shall, in addition to the penalties provided in this title, be liable to a penalty equal to the total amount of refunds which was not refunded to the employee resulting from any excess of the amount withheld over the tax actually due on their return. (*Sec. 252, NIRC, as amended*)

2. VALUE ADDED TAX (VAT)

a. CONCEPT AND ELEMENTS OF VATABLE TRANSACTIONS

Definition of VAT

VAT is a form of sales tax. It is a tax on consumption levied on the sale, barter, exchange or lease of goods or properties and services in the Philippines, and on importation of goods into the Philippines. It is an indirect tax, which may be shifted or passed on the buyer, transferee or lessee of goods, properties or services. (*Sec. 105, NIRC, as amended*)

VAT is a form of sales tax that is borne by the end-user or consumer. It is imposed on each sale of goods or services in the course of trade or business, or on importation of goods, as they pass along the production and distribution chain. (*Team Energy Corporation (formerly: Mirant Pagbilao Corporation and Southern Energy Quezon, Inc.) vs. CIR, G.R. No. 197663, March 14, 2018*)

It is the amount of tax paid on the goods, properties or services bought, transferred, or leased may be shifted or passed on by the seller, transferor, or lessor to the buyer, transferee or lessee. Unlike a direct tax, such as the income tax, which primarily taxes an individual's ability to pay based on his income or net wealth, an indirect tax, such as the VAT, is a tax on consumption of goods, services, or certain transactions involving the same. The VAT, thus, forms a substantial portion of consumer expenditures. (*Contex vs. CIR, G.R. No. 151135 dated July 2, 2004*)

Further, in indirect taxation, there is a need to distinguish between the liability for the tax and the burden of the tax. In adding or including the VAT due to the selling price, the seller remains the person primarily and legally liable for the payment of the tax. What is shifted only to the intermediate buyer and ultimately to the final purchaser is the burden of the tax. (*Ibid.*)

Stated differently, a seller who is directly and legally liable for payment of an indirect tax, such as the VAT on goods or services is not necessarily the person who ultimately bears the burden of the same tax. It is the final purchaser or consumer of such goods or services who, although not directly and legally liable for the payment thereof, ultimately bears the burden of the tax. (*Ibid.*)

Basic Characteristics of VAT

The following are the basic characteristics of VAT:

1. It is a broad-based tax on consumption of goods, properties, or services in the Philippines as it applies to all stages of manufacture,

ARELLANO UNIVERSITY SCHOOL OF LAW BAR OPERATIONS COMMISSION 2025

production, and distribution of goods and services.

2. It is an indirect tax.
3. There is no cascading in the value added tax system and is thus not considered a tax on tax.
4. It is a tax on the value added by the taxpayer.
5. The VAT liability is arrived at using the tax credit or invoice method, where "an entity can credit against or subtract from the VAT charged on its sales or outputs the VAT paid on its purchase, inputs and imports. (*CIR vs. Seagate Technology (Philippines)*, G.R. No. 153866 dated February 11, 2005)

Elements of a VATable Transaction:

1. There must be a sale, barter, exchange, lease of good or properties, or rendering of service in the Philippines;
2. It must be done in the ordinary course of trade or business;
3. The transaction is done in the Philippines; and
4. It must not be exempt. (*Sec. 105, NIRC, as amended*)

Sale, barter, exchange, lease of good or properties, or rendering of service

Republic Act No. 11976 or the Ease of Paying Taxes (EOPT), adopts the accrual basis of recognizing sales for both sales of goods and services. Hence, all reference to "gross selling price", "gross value in money", and "gross receipts" shall now be referred to as the "gross sales", regardless whether the sale is for goods under Section 106 or for services under Section 108 of the Tax Code. (*RR No. 03-2024*)

The allocation of condominium units to partners of a joint venture or consortium formed for the purpose of undertaking construction projects as a return on their contribution is not subject to VAT because such

allocation is not a sale, barter or exchange of real property done in the ordinary course of business. A joint venture for the purpose of undertaking construction projects, according to the BIR, is not a taxable corporation under Section 22(B) of the Tax Code, and the assignment by the owner to developer of the latter's share in the developed lots under a memorandum of sharing is not VAT since the owner, by contributing his property neither sells, barter or exchanges goods or properties nor renders any service subject to VAT. However, **the subsequent disposition by the co-venturers of the areas allocated to them shall be subject to VAT, among other taxes.** (*Malayan Insurance Company Inc. vs. St. Francis Square Realty*, G.R. Nos. 198916-17, July 23, 2018)

Under RA No. 4746 or "The Condominium Act", the corporate purposes of a condominium corporation are limited to holding the common areas, either in ownership or any other interest in real property recognized by law; management of the project; and to such other purposes necessary, incidental, or convenient to the accomplishment of these purposes. Additionally, Section 10 prohibits the articles of incorporation or by-laws of the condominium corporation from containing any provisions contrary to the provisions of RA 4726, the enabling or master deed, or the declaration of restrictions of the condominium project. (***In the Matter of Declaratory Relief on the Validity of BIR RMC No. 65-2012, GR No. 215801, January 15, 2020, Lazaro-Javier, J.***)

In sum, the collection of association dues, membership fees, and other assessments/charges is purely for the benefit of the condominium owners. It is a necessary incident to the purpose to effectively oversee, maintain, or even improve the common areas of the condominium as well as its governance. Hence, condominium corporations are not engaged in trade or business. (***Ibid.***)

Rule on Regularity

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The phrase "in the course of trade or business" means the regular conduct or pursuit of a commercial or an economic activity, including transactions incidental thereto, by any person regardless of whether or not the person engaged therein is a non-stock, nonprofit private organization (irrespective of the disposition of its net income and whether or not it sells exclusively to members or their guests), or government entity. (*Sec. 105, NIRC, as amended; RR No. 16-2005*)

Isolated transactions, or those not made in the regular course of trade or business, are therefore not subject to VAT (*BIR Ruling No. 113-98*)

VAT is not imposed on every transaction but depends on the taxpayer's role in the production chain. Under Section 105 of the Tax Code, it applies only to the sale, barter, or exchange of goods or services done in the course of trade or business. Transactions outside this scope may incidentally contribute to the production chain but do not generate output VAT, nor allow for proper VAT crediting, as these arise only through the ordinary course of trade or business. (*CIR vs. Magsaysay Lines, Inc., G.R. No. 146984, July 28, 2006*)

For VAT purposes, it is immaterial if a corporation's primary purpose states that it renders services to affiliates on a reimbursement-cost basis without profit; what matters is that services are provided for a fee, remuneration, or consideration, making them subject to VAT. (*CIR vs. CA and Commonwealth Management and Services Corporation, G.R. No. 125355, March 30, 2000*)

The sale of the power plants is a governmental function mandated by law to privatize NPC generation assets, not a commercial or economic activity; therefore, it is not subject to VAT. (*Power Sector Assets and Liabilities Management Corporation vs. CIR, G.R. No. 198146, August 08, 2017*)

Membership fees, assessment dues, and similar charges are not subject to VAT because

they do not involve a sale of services or goods. These payments are used for the club's operations and maintenance, not for commercial transactions, and thus do not constitute economic activity under the Tax Code. (*Association of Non-Profit Clubs, Inc. vs. Bureau of Internal Revenue, G.R. No. 228539, June 26, 2019*)

Association dues, membership fees, and other assessments/charges do not arise from transactions involving the sale, barter, or exchange of goods or property. Nor are they generated by the performance of services. As such, they are not subject to VAT.

Case law provides that membership fees, assessment dues, and the like collected by recreational clubs are not subject to value-added tax "because in collecting such fees, the club is not selling its service to the members. Conversely, the members are not buying services from the club when dues are paid; hence, there is no economic or commercial activity to speak of as these dues are devoted for the operations/maintenance of the facilities of the organization. As such, there could be no "sale, barter or exchange of goods or properties, or sale of a service" to speak of, which would then be subject to VAT under the 1997 NIRC. (***In the Matter of Declaratory Relief on the Validity of BIR RMC No. 65-2012, GR No. 215801, January 15, 2020, Lazaro-Javier, J.***)

Rule of Regularity under Section 105 of the Tax Code does not apply to the following:

1. Sale of services by a non-resident

It shall be considered as being rendered in the course of trade and business, even if the performance of services is not regular. (*RR No. 16-2005*)

The VAT shall be withheld by the payor before remitting the service fees payable to the non-resident alien. (*Sec. 105, NIRC, as amended*)

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ARELLANO UNIVERSITY SCHOOL OF LAW BAR OPERATIONS COMMISSION 2025

NOTE: Digital services delivered by resident digital services providers are considered performed or rendered in the Philippines if the digital services are consumed in the Philippines (*VAT on Digital Services, RA No. 12023*)

2. Importation

Any person who imports goods shall be subject to VAT whether or not made in the course of the business. (*Ibid*)

Any business where the gross sales do not exceed P100,000 during the 12 month period shall be considered principally for subsistence or livelihood and not in the course of trade or business. They are exempt from VAT and percentage tax.

3. Transactions deemed sales

Please see discussion VIII. TAXATION LAW > B. National Internal Revenue Code of 1997 (NIRC), as amended by R.A. No. 10963, or the Tax Reform for Acceleration and Inclusion (TRAIN) Law Taxes and R.A. No. 11976 or the Ease of Paying Taxes Act > Value-Added Tax (VAT) > a. Transactions Deemed Sale Subject to VAT.

The transaction is done in the Philippines

VAT system uses the destination principle as a basis for the jurisdictional reach of the tax. Goods and services are taxed only in the country where they are consumed. (*CIR vs. American Express International, Inc. G.R. No. 152609, June 29, 2005*)

Please see additional discussions VIII. TAXATION LAW > B. National Internal Revenue Code of 1997 (NIRC), as amended by R.A. No. 10963, or the Tax Reform for Acceleration and Inclusion (TRAIN) Law Taxes and R.A. No. 11976 or the Ease of Paying Taxes Act > 2. Value-Added Tax (VAT) > c. Destination Principle and Cross-Border Doctrine.

It must not be exempt

Persons required to register for VAT:

1. Any person who, in the course of his trade or business, sells, barter, exchanges or leases goods or properties, or renders services, shall be liable to VAT if:

(a) Gross sales for the past twelve (12) months, other than those that are exempt under Section 109(A) to (BB) have exceeded three million pesos (P3,000,000); **OR**

(b) There are reasonable grounds to believe that his gross sales for the next twelve (12) months, other than those that are exempt under Section 109(A) to (CC), will exceed three million pesos (P3,000,000) (*Sec. 236(G), NIRC, as amended*)

2. Any person who imports goods, whether the importer is an individual or corporation and whether or not made in the course of trade or business (*RR No. 16-2005*)

A taxpayer may elect to register for VAT. However, a taxpayer who voluntarily registers as VAT shall not be entitled to cancel his/her VAT registrations for the next three (3) years. (*Sec. 236(G), NIRC, as amended*)

Every person who becomes a VAT registered shall register, either electronically or manually, with the appropriate Revenue District Office, as determined by the Commissioner. Failure to register, he shall be liable to pay the tax as if he were a VAT-registered person, but without the benefit of input tax credits for the period in which he was not properly registered. (*Sec. 236(F), NIRC, as amended*)

Transactions subject to VAT

Under the Tax Code, there are three types of transactions subject to VAT:

1. Sale, Barter, Exchange, or Lease of goods or properties
2. Sale or Exchange of Services; and
3. Importation of Goods (*Sec. 105(A), NIRC, as amended*).

Sale, Barter, or Exchange of Goods or Properties

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ARELLANO UNIVERSITY SCHOOL OF LAW BAR OPERATIONS COMMISSION 2025

There shall be levied, assessed and collected on every sale, barter or exchange of goods or properties, VAT equivalent to twelve percent (12%) of the gross sales of the goods or properties sold, bartered or exchanged, to be paid by the seller or transferor. (*Sec. 106, NIRC, as amended*)

Definition of "Goods" or "Properties" for VAT purposes

The term "goods" or "properties" shall mean all tangible and intangible objects which are capable of pecuniary estimation and shall include:

- (a) Real properties held primarily for sale to customers or held for lease in the ordinary course of trade or business;
- (b) The right or the privilege to use patent, copyright, design or model, plan, secret formula or process, goodwill, trademark, trade brand or other like property or right;
- (c) The right or the privilege to use in the Philippines of any industrial, commercial or scientific equipment;
- (d) The right or the privilege to use motion picture films, tapes and discs; and
- (e) Radio, television, satellite transmission and cable television time. (*Sec. 106(A)(1), NIRC, as amended*)

Definition of Gross Sales for VAT purposes

The term "gross sales" means the total amount of money or its equivalent value in money which the purchaser pays or is obligated to pay to the seller in consideration of the sale, barter or exchange of the goods or properties, excluding the value-added tax. The excise tax, if any, on such goods or properties shall form part of the gross sales. (*Sec. 106(A)(1), NIRC, as amended*)

In the case of sale, barter or exchange of real property subject to VAT, gross sales shall mean the consideration stated in the sales document

or the fair market value, whichever is higher. If the VAT is not billed separately in the document of sale, the selling price or the consideration stated therein shall be deemed to be inclusive of VAT. (*Sec. 4, RR No. 04-2007*)

Sales Returns, Allowances, and Discounts

In computing the taxable sales/selling price, sales returns and allowances and sales discount may be deducted from gross sales/selling price. However, for a sales discount to be deductible, it must be:

- i. Granted at the time of sales;
- ii. Indicated in the invoice; and
- iii. Not be dependent upon the happening of a future event (*Sec. 106(D), NIRC, as amended*)

Sale or exchange of services

The phrase "sale or exchange of services" means the performance of all kinds of services in the Philippines for others for a fee, remuneration or consideration, regardless of whether or not the performance of the service calls for the exercise or use of the physical or mental faculties. (*Sec. 108(A), NIRC, as amended*)

Definition of Gross Sales

"Gross sales" means the total amount of money or its equivalent representing the contract price, compensation, service fee, rental or royalty, including the amount charged for materials supplied with the services and deposits and advanced payments actually or constructively received during the taxable quarter for the services performed or to be performed for another person, which the purchaser pays or is obligated to pay to the seller in consideration of the sale, barter, or exchange of services that has already been rendered by the seller and the use or lease of properties that have already been supplied by the seller, excluding value-added tax and those amounts earmarked for payment to third (3rd) party or received as reimbursement for payment on behalf of another which do not redound to the benefit of the seller as provided

ARELLANO UNIVERSITY SCHOOL OF LAW BAR OPERATIONS COMMISSION 2025

under relevant laws, rules or regulation. Provided that, for long-term contracts for a period of one (1) year or more, the invoice shall be issued on the month in which the service, or use or lease of properties is rendered or supplied. (*Sec. 108(A), NIRC, as amended*)

VAT on both sale of goods or properties, and sale of services and lease of properties shall be based on "gross sales." (*EOPT Act*)

Since the VAT on sales of services and lease of properties will be based on "gross sales", the taxpayers are now required to remit the output VAT upon accrual of sale **regardless of when the actual collection took place.**

VAT on sales of goods	VAT on sales of services
It accrues upon consumption of the sales regardless of the terms of payment	It accrues upon actual and constructive receipt of payment, regardless whether the services have been performed.

Payments to Medical Providers

Only the portion representing compensation for the HMO's services (i.e. acting as intermediary between its members and healthcare providers, pre-arranging medical services, providing guarantee for necessary deposits, bonds, and other costs) should form part of its gross receipts subject to VAT. An HMO is not liable for VAT on the portion earmarked for its members' medical utilization, which the HMO eventually pays to its accredited healthcare providers.

These funds are merely held in trust by the HMO as administrator, and its inchoate right of ownership in relation to the same would ripen into actual ownership only if there is underutilization of the membership fees at the end of the fiscal year. Thus, the total amount received by a health maintenance organization (HMO from its members, undiminished by any amount paid or payable to the owners and

operators of its partner hospitals, clinics, and medical practitioners should not form part of its gross receipts for purposes of VAT. (*Medicaid Philippines, Inc. vs. Commissioner of Internal Revenue, G.R. No. 222743, April 5, 2017*)

NOTE: Upon effectivity of EOPT Act, all references to "gross receipts" shall now be referred to as the "gross sales". The case of MEDICARD was decided prior to the enactment of the EOPT Act.

Importation of Goods

In general, there shall be levied, assessed and collected on every importation of goods a value-added tax equivalent to twelve percent (12%) whether for use in business or not. (*Sec. 107(A), NIRC, as amended*)

Tax Base for Importation of Goods

The VAT is based on the total value used by the Bureau of Customs (BOC) in determining tariff and customs duties plus customs duties, excise taxes, if any, and other charges. Provided, That where the custom duties are determined on the basis of the quantity or volume of the goods, the VAT shall be based on the landed cost plus excise taxes, if any. (*Sec. 107(A), NIRC, as amended*)

Import VAT Liability

As a general rule, the VAT shall be paid by the importer prior to the release of such goods from customs custody. (*Sec. 107(A), NIRC, as amended*)

In case of tax-free importation, the non-exempt person to whom the imported goods were subsequently sold, exchanged, or transferred shall be considered the importer thereof. As such, said non-exempt person shall be liable for the VAT. The tax due on the importation shall constitute a lien on the goods, superior to all other charges, irrespective of the possessor. (*Sec. 107, NIRC, as amended*)

b. IMPACT AND INCIDENCE OF TAXATION

The VAT is an indirect tax. As such, the amount of tax paid on the goods, properties or

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services bought, transferred, or leased may be shifted or passed on by the seller, transferor, or lessor to the buyer, transferee or lessee. (*Contex vs. CIR, GR No. 151135 dated July 2, 2004*)

In indirect taxation, there is a need to distinguish between the **liability for the tax** and the **burden of the tax**. [T]he amount of tax paid may be shifted or passed on by the seller to the buyer. What is transferred in such instances is not the liability for the tax, but the tax burden. In adding or including the VAT due to the selling price, the seller remains the person primarily and legally liable for the payment of the tax. What is shifted only to the intermediate buyer and ultimately to the final purchaser is the burden of the tax. Stated differently, a seller who is directly and legally liable for payment of an indirect tax, such as the VAT on goods or services is not necessarily the person who ultimately bears the burden of the same tax. It is the final purchaser or consumer of such goods or services who, although not directly and legally liable for the payment thereof, ultimately bears the burden of the tax. (*Id.*)

Impact of Taxation	Incidence of Taxation
The point on which the tax is originally imposed.	The point on which the tax burden ultimately rests.
In the case of VAT, it shall be the vendor who is liable. (<i>Sec. 105, NIRC, as amended</i>)	In the case of VAT, it shall be the consumer who ultimately bears the burden of tax. (<i>Sec. 105, NIRC, as amended</i>)

c. DESTINATION PRINCIPLE; CROSS-BORDER DOCTRINE

Under the Destination Principle, goods and services are **taxed only in the country where these are consumed**.

Meanwhile, the Cross Border Doctrine mandates that **no VAT shall be imposed to form part of the cost of goods destined for consumption outside the territorial border** of the taxing authority. (*Atlas Consolidated Mining and Development Corp. vs. CIR, G.R. Nos. 141104 & 148763, June 08, 2007; CIR vs. Filminera Resources Corp., G.R. No. 236325 dated September 16, 2020*)

Hence, actual export of goods and services from the Philippines to a foreign country must be free of VAT, while those destined for use or consumption within the Philippines shall be imposed with VAT. Plainly, sales of export products to another producer or to an export trader are subject to zero percent rate provided the export products are actually exported and consumed in a foreign country. (*Ibid.*)

Exception to the Destination Principle

For the supply of service to be zero-rated to be an exception, the law requires that:

1. The service to be performed in the Philippines;
2. The service fall under any of the categories in Section 102(b) of the Tax Code; and
3. It be paid in acceptable foreign currency accounted for in accordance with BSP rules and regulations. (*Commissioner of Internal Revenue vs. American Express International, Inc., G.R. No. 152609, June 29, 2005*)

Ecozones and Freeport Zones

Prior to the CREATE Act, the sale of goods and services by a VAT-registered seller to registered enterprises in ecozones and freeport zones were treated as a constructive export. Ecozones and Freeport zones were, by legal fiction, regarded as foreign territories (*RMC No. 74-1999 and RMC No. 7-2007*).

With the passage of CREATE Act, is the cross border doctrine still applicable for purposes of VAT as laid down in RMC No. 74-1999 and RMC No. 50-2007?

The "cross border doctrine" as applied to Ecozones or Freeport zones has been

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ARELLANO UNIVERSITY SCHOOL OF LAW BAR OPERATIONS COMMISSION 2025

rendered ineffectual and inoperative for VAT purposes because of the following:

- i. Passage of RA No. 11534, or the CREATE Act, expressly providing that only those goods and services that are directly and exclusively used in the **registered project or activity of registered business enterprises (RBEs)** qualify as VAT 0% local purchases;
- ii. Sections 294(E) and 295(D), Title XIII of the Tax Code, as amended by the CREATE Act, and as implemented under Rule 2, Section 5, and Rule 18, Section 5, respectively, of the CREATE IRR, stating certain parameters for the availment of VAT zero-rating on local purchases of registered export enterprises, regardless of location; and
- iii. Issuance of RR No. 21-2021, amending Sections 4.106-5(b) and 4.108-5(b.2) of RR No. 16-2005, as amended, to harmonize the VAT zero-rate provisions of the Tax Code, as amended by TRAIN and CREATE laws, which now provide that the effectively zero-rated sales shall only apply to sales of goods and services rendered to persons or entities who have direct and indirect tax exemption granted pursuant to special laws or international agreements to which the Philippines is a signatory. (*Q&A No. 1, RMC No. 24-2022*)

d. TRANSACTIONS DEEMED SALE SUBJECT TO VAT

The following transactions shall be deemed sale:

- i. Transfer, use or consumption, not in the course of business of goods or properties originally intended for

sale or for use in the course of business;

- ii. Distribution or transfer to:
 - a. Shareholders or investors as share in the profits of the VAT registered persons; or
 - b. Creditors in payment of debt;
- iii. Consignment of goods if actual sale is not made within sixty **(60) days** following the date such goods were consigned; and
- iv. Retirement from or cessation of business with respect to inventories of taxable goods existing as of such retirement or cessation, whether or not the business is continued by the new owner or successor. (*Sec. 106(B), NIRC, as amended*)

e. ZERO-RATED TRANSACTIONS

It is a sale, barter or exchange of goods, properties and/or services subject to zero percent (0%) VAT. (*Sec. 106(A)(2) and Sec. 108(B), NIRC, as amended*)

It is a taxable transaction for VAT purpose, but shall not result in any output tax. However, the input tax on purchases of goods, properties or services, related to such zero-rated sales, may be available as tax credit or refund. (*R.R. No. 16-2005*)

Distinguish Zero-Rated Sales from VAT-Exempt Sales

Zero-Rated Sale	VAT Exempt Sale
<i>As to Output Tax</i>	
Taxable transaction but does not result in an output tax.	Not subject to the output tax.
<i>As to Input Tax</i>	
Input VAT on the purchases of a VAT-registered person with zero-rated sales may be refunded.	Seller in an exempt transaction is not entitled to any input tax on his purchases despite the issuance

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ARELLANO UNIVERSITY SCHOOL OF LAW BAR OPERATIONS COMMISSION 2025

	of a VAT invoice or receipt.
As to Registration	
Persons engaged in transactions which are zero-rated, being subject to VAT, are required to register.	Registration is optional for VAT-exempt persons.

(CIR vs. Cebu Toyo Corp. GR No. 149073 dated February 16, 2005)

Distinguish zero-rated, effectively zero-rated, and VAT exempt transactions

Zero-rated	Effectively Zero-Rated	VAT Exemptions
Source are export sales, including those deemed export sales	Source are special laws and other international agreements (where PH is signatory)	Source is just the NIRC and amending laws.
Intended to be enjoyed by the SELLER who is directly and legally liable for the VAT, making such seller internationally competitive by allowing the refund or credit of input taxes that are attributable to export sales	Intended to benefit the BUYER who, not being directly and legally liable for the payment of the VAT, will ultimately bear the burden of the tax shifted by the suppliers	In exemption, there is only partial relief because the purchaser is not allowed any tax refund of or credit for input taxes paid
Total Relief from Tax Burden		Partial Relief
Tax Credit/Refund is ALLOWED		Tax Credit/Refund is NOT ALLOWED

Zero-rated	Effectively Zero-Rated	VAT Exemptions
No need to apply with the BIR for zero-rating because it's already provided for in the NIRC*		No need to apply for VAT exemption since it's already provided in the NIRC*

(CIR vs. Seagate Technology [Philippines], G.R. No. 153866, February 11, 2005)

Transactions considered as zero-rated sales:

The following sales (of goods or properties) by VAT-registered persons shall be subject to zero-percent (0%) rate:

a. Export Sales - The term "export sales" means:

i. The sale and actual shipment of goods from the Philippines to a foreign country, irrespective of any shipping arrangement that may be agreed upon which may influence or determine the transfer of ownership of the goods so exported and paid for in acceptable foreign currency or its equivalent in goods or services, and accounted for in accordance with the rules and regulations of the BSP;

ii. Sale of raw materials and packaging materials to a non-resident buyer, for delivery to a resident local export-oriented enterprise, to be used in the manufacturing, processing, packing, or repacking in the Philippines of the said buyer's goods, and paid for in acceptable foreign currency and accounted for in accordance with the rules and regulations of the BSP;

iii. Sale of raw materials or packaging materials to an export-oriented enterprise whose export sales exceed 70% of its total annual production

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ARELLANO UNIVERSITY SCHOOL OF LAW BAR OPERATIONS COMMISSION 2025

iv. Sales considered as export sales under Executive Order No. 226 otherwise known as the "Omnibus Investment Code of 1987" and other special laws.

v. Sale of goods, supplies, equipment, and fuel to persons engaged in international shipping or air transport operations; provided that the same shall be used for international shipping or air transport operations.

b. Sales to persons or entities whose exemption under special laws or international agreements to which the Philippines is a signatory effectively subjects such sales to zero rate.

c. Sales to offshore gaming licensees subject to gaming tax under Section 125-A of the NIRC.

d. Those sales subject to zero percent (0%) VAT under special laws. (*Sec. 106(B), NIRC, as amended*)

Under Section 108(B) of the NIRC, the following **services** performed in the Philippines by VAT-registered persons shall be subject to zero percent (0%) VAT rate:

1. Processing, manufacturing or repacking goods for other persons doing business outside the Philippines which goods are subsequently exported, where the services are paid for in acceptable foreign currency and accounted for in accordance with the rules and regulations of the BSP;
2. Services other than those mentioned in the preceding paragraph, rendered to a person engaged in business conducted outside the Philippines **OR** to a nonresident person not engaged in business who is outside the Philippines when the services are performed, the consideration for which is paid for in acceptable foreign currency and accounted for

in accordance with the rules and regulations of the BSP;

3. Services rendered to persons or entities whose exemption under special laws or international agreements to which the Philippines is a signatory effectively subjects the supply of such services to zero percent (0%) rate;
4. Services rendered to persons engaged in international shipping or air transport operations, including leases of property for use thereof; provided that these services shall be exclusive for international shipping or air transport operations.

NOTE: The services referred to herein shall not pertain to those made relative to their transport of passengers, goods or cargoes from one place in the Philippines to another place in the Philippines, the same being subject to twelve percent (12%) VAT under Sec. 108 of the Tax Code;

5. Services performed by contractors and/or subcontractors in processing, converting, or manufacturing goods for an export-oriented enterprise whose export sales is at least seventy percent (70%) of the total annual production.
6. Transport of passengers and cargo by domestic air or sea vessels from the Philippines to a foreign country.
7. Sale of power or fuel generated through renewable sources of energy such as, but not limited to, biomass, solar, wind, hydropower, geothermal and steam, ocean energy, and other emerging sources using technologies such as fuel cells and hydrogen fuels.

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ARELLANO UNIVERSITY SCHOOL OF LAW BAR OPERATIONS COMMISSION 2025

8. Services rendered to offshore gaming licensees subject to gaming tax under Section 125-A of the NIRC.

As a general rule, the VAT system uses the destination principle as a basis for the jurisdictional reach of the tax. Goods and services are taxed only in the country where they are consumed. Thus, exports are zero-rated, while imports are taxed. (*CIR vs. American Express International, Inc.*, G.R. No. 152609, June 29, 2015)

The law clearly provides for an exception to the destination principle; that is, for a zero percent VAT rate for services that are performed in the Philippines, "paid for in acceptable foreign currency and accounted for in accordance with the rules and regulations of the [BSP]." (*Ibid*)

Thus, for the supply of service to be zero-rated as an exception, the law merely requires that:

- i. Service be performed in the Philippines;
- ii. Service fall under any of the categories in Section 102(b) of the Tax Code; and
- iii. It be paid in acceptable foreign currency accounted for in accordance with BSP rules and regulations. (*Ibid*)

To qualify for VAT zero-rating, Section 108 (B)(2) requires the concurrence of the four conditions:

- i. Services rendered should be other than "processing, manufacturing or repacking of goods;
- ii. Services are performed in the Philippines;
- iii. Service-recipient is (a) a person engaged in business conducted

outside the Philippines; or (b) a non-resident person not engaged in a business which is outside the Philippines when the services are performed; and

- iv. Services are paid for in acceptable foreign currency inwardly remitted and accounted for in conformity with BSP rules and regulations [*Chevron Holdings, Inc. (formerly Caltex Asia Limited) vs. CIR, G.R. No. 215519, July 05, 2022*]

Anent the third requisite, the Court emphasized in *CIR vs. Deutsche Knowledge Services Pte. Ltd.* that for sales to a non-resident foreign corporation to qualify for zero-rating, the following must be proved: (1) that their client was established under the laws of a country, not the Philippines or, simply, is not a domestic corporation; and (2) that it is not engaged in trade or business in the Philippines. (*Ibid*)

To be sure, there must be sufficient proof of both of these components: showing not only that the clients are foreign corporations, but also are not doing business in the Philippines. (*Ibid*)

Therefore, the taxpayer-claimant must present, at the very least, both the SEC Certificates of Non-Registration – to prove that the affiliate is foreign; and the Articles or Certificates of Foreign Incorporation, printed screenshots of US SEC website showing the state/province/country where the entity was organized, or any similar document – to prove the fact of not engaging in trade or business in the Philippines at the time the sales are rendered. (*Ibid.*)

World Health Organization (WHO), the contractee, is exempt from direct and indirect taxes pursuant to an international agreement where the

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ARELLANO UNIVERSITY SCHOOL OF LAW BAR OPERATIONS COMMISSION 2025

Philippines is a signatory. The exemption from indirect taxes should mean that the entity or person exempt is the contractor itself because the manifest intention of the agreement is to exempt the contractor so that no tax may be shifted to the contractee. The immunity of WHO from indirect taxes extends to the contractor by treating the sale of services as effectively zero-rated. (*CIR vs. John Gotamco & Sons, Inc.*, G.R. No. L-31092, February 27, 1987)

f. VAT-EXEMPT PERSONS vs. VAT-EXEMPT TRANSACTIONS

Definition of VAT exempt Transaction

These refer to the sale of goods or properties and/or services and the use or lease of properties that is not subject to VAT. The person making the exempt sale of goods, properties or services shall not bill or pass on any output tax to his customers because the said transaction is not subject to VAT.

However, the seller is not allowed to credit the VAT (input tax) passed to him on his purchases of taxable goods, properties or services, because he has no output tax to deduct it from. (*Sec. 109, NIRC, as amended*)

In other words, since the seller is not subject to output tax, it is likewise not allowed any tax credit of input tax from purchases.

Definition of VAT exempt sale

An exemption means that the sale of goods or properties and/or services and the use or lease of properties is not subject to VAT (output tax) and the seller is not allowed any tax credit on VAT (input tax) previously paid.

The person making the exempt sale of goods, properties or services shall not bill any output tax to his customers because the said transaction is not subject to VAT. On the other hand, a VAT-registered purchaser of VAT-exempt goods/properties or services which are exempt from VAT is not entitled to any input

tax on such purchase despite the issuance of a VAT invoice or receipt. (*Contex Corporation vs. CIR*, G.R. No. 151135, July 02, 2014)

Distinguish VAT-exempt transaction from VAT exempt person

VAT-exempt transaction	VAT-exempt person
An exempt transaction , involves goods or services which, by their nature, are specifically listed in and expressly exempted from the VAT under the Tax Code, without regard to the tax status of the party to the transaction.	An exempt party , on the other hand, is a person or entity granted VAT exemption under the Tax Code, a special law or an international agreement to which the Philippines is a signatory, and by virtue of which its taxable transactions become exempt from the VAT.
Such transaction is not subject to the VAT, but the seller is not allowed any tax refund of or credit for any input taxes paid.	Such party is also not subject to the VAT, but may be allowed a tax refund of or credit for input taxes paid, depending on its registration as a VAT or non-VAT taxpayer.

(*CIR vs. Seagate Technology Philippines; G.R. No. 153866; February 11, 2005*)

VAT-exempt Transactions:

The following transactions shall be exempt from the value-added tax:

- a. Sale or importation of the following:
 - i. Agricultural and marine food products in their original state. This includes products that have

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ARELLANO UNIVERSITY SCHOOL OF LAW BAR OPERATIONS COMMISSION 2025

- undergone simple processes of preparation or preservation, such as freezing, drying, salting, roasting, smoking, or stripping;
- ii. Livestock and poultry for, or producing foods for, human consumption, breeding stock, and genetic materials therefor;
 - b. Sale or importation of fertilizers; seeds, seedlings, and fingerlings; fish, prawn, livestock, and poultry feeds, including ingredients, whether locally produced or imported, used in the manufacture of finished feeds (except specialty feeds for race horses, fighting cocks, aquarium fish, zoo animals and other animals generally considered as pets);
 - c. Importation of personal and household effects belonging to residents returning from abroad and non-residents resettling in the Philippines; Provided, that such goods are exempt from customs duties;
 - d. Importation of professional instruments and implements, tools of trade, wearing apparel, domestic animals, and personal and household effects belonging to overseas Filipinos or their families, in quantities and of the class suitable to the profession, rank, or position of the person importing, for their own use and not for barter or sale. Said items must accompany the person importing or arrive within a reasonable time;
 - e. Services subject to percentage tax under Title V;
 - i. Domestic carriers by land for the transport of passengers and keepers of garages (Sec. 117);
 - ii. International air and shipping carriers (Sec. 118);
 - iii. Franchise grantees of radio and/ or television broadcasting whose annual gross receipts of the preceding year do not exceed P10,000,000.00, and gas and water utilities (Sec. 119);
 - iv. Overseas dispatch, message or conversation emanating from the Philippines (Sec. 120);
 - v. Life insurance companies (Sec. 123);
 - vi. Fire/ marine/ or miscellaneous insurance agents of foreign insurance companies (Sec. 124);
 - vii. Cockpits/ cabarets/night or day clubs/boxing exhibitions, professional basketball games, Jai-Alai and race tracks (Sec. 125); and
 - viii. Initial public offering (IPO) and sale of publicly-listed shares (Sec. 127)
 - f. Services by agricultural contract growers, and milling for others of palay into rice, corn into grits and sugar cane into raw sugar;
 - g. Medical, dental, hospital, and veterinary^[1] services except those rendered by professionals;
 - h. Educational services rendered by:
 - i. Private educational institutions duly accredited by the Department of Education (DepEd), the Commission on Higher Education (CHED), or the Technical Education and Skills Development Authority (TESDA); and
 - ii. Government educational institutions
 - i. Services rendered by individuals pursuant to an employer-employee relationship;

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ARELLANO UNIVERSITY SCHOOL OF LAW BAR OPERATIONS COMMISSION 2025

- j. Services rendered by regional or area headquarters established in the Philippines by multinational corporations, which act as supervisory, communications, and coordinating centers for their affiliates, subsidiaries, or branches in the Asia-Pacific Region and do not earn or derive income from the Philippines;
- k. Transactions exempt under international agreements to which the Philippines is a signatory or special laws, except those under P.D. No. 529;
- l. Sales by agricultural cooperatives duly registered with the Cooperative Development Authority (CDA) to their members; sales of their produce, whether in its original state or processed form, to non-members; and importation of direct farm inputs, machinery and equipment, including spare parts, to be used directly and exclusively in their production;
- m. Gross receipts from lending activities by credit or multi-purpose cooperatives duly registered with the CDA;
- n. Sales by non-agricultural, non-electric, and non-credit cooperatives duly registered with the CDA, where the capital contribution of each member does not exceed P15,000, regardless of the aggregate capital and net surplus ratably distributed among members;

Note that unlike Section 109(L), there are no qualifications as to the product and the buyer. Under Section 109(L), sale by agricultural cooperatives is subject to VAT, unless:

- i. The sale is made to a member; or
 - ii. The sale is made to a non-member and the goods sold are the cooperative's produce.
- o. Export sales by persons who are not VAT-registered;
- Note that export sales by a VAT-registered person is zero rated, not exempt.
- p. Sale of the following real properties:
- i. Real properties not primarily held for of trade or business; sale or for lease in the ordinary course
 - ii. Real properties utilized for low-cost and socialized housing, as defined under Republic Act No. 7279 or the "Urban Development and Housing Act of 1992" and other related laws;
 - iii. Residential lot valued at P2.5 million and below; and
 - iv. House and lot, and other residential dwellings, valued at P4.2 million and below.

Provided, that beginning January 1, 2024 and every three years thereafter, the amounts herein stated shall be adjusted to present values using the Consumer Price Index, as published by the Philippine Statistics Authority.

Note: Beginning January 1, 2024, the VAT exemption threshold for sale of house and lot, and other residential dwellings shall be **P3,6000,000** (*R.R. No. 1-2024*)

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ARELLANO UNIVERSITY SCHOOL OF LAW BAR OPERATIONS COMMISSION 2025

- q. Lease of residential unit with monthly rental not exceeding P15,000;

Note that lease of commercial units is not VAT exempt.

Monthly Rental	Annual Gross Receipt	VAT
Not exceeding P15,000	Not exceeding P3,000,000	Exempt under Sec. 109 (Q)
	Exceeding P3,000,000	Exempt under Sec. 109 (Q)
Exceeding P15,000	Not exceeding P3,000,000	Exempt under Sec. 109 (CC) but subject to 3% other percentage tax under Sec. 116
	Exceeding P3,000,000	Not exempt

- r. Sale, importation, and printing or publication of books and newspaper, magazine, journal, review bulletin, or any such educational reading material covered by the UNESCO Agreement on the Importation of Educational, Scientific and Cultural Materials, including the digital or electronic format thereof, unless such materials are principally devoted to the publication of paid advertisements;
- s. Transport of passengers by international carriers;

Note that transport of passengers to a foreign country by a domestic carrier is zero-rated, not exempt.

- t. Sale, importation, or lease of passenger or cargo vessels and aircraft, including engine, equipment, and spare parts thereof for domestic or international transport operations;
- u. Importation of fuel, goods, and supplies by persons engaged in international shipping or air transport operations; provided that the same shall be used for international shipping or air transport operations;
- v. Note that if the transaction is a sale to persons engaged in international shipping or air transport operations, it is zero-rated, not exempt.
- w. Services of bank and non-bank financial intermediaries;
- x. Sale or lease of goods and services to senior citizens and persons with disability, as provided under Republic Act Nos. 9994 (Expanded Senior Citizens Act of 2010) and 10754 (An Act Expanding the Benefits and Privileges of Persons With Disability, respectively);
- y. Transfer of property pursuant to Section 40(C)(2) of the Tax Code;
- z. Association dues, membership fees, and other assessments and charges collected by homeowners' associations and condominium corporations;
- aa. Sale of gold to the Bangko Sentral ng Pilipinas (BSP);
- bb. Sale or importation of prescription drugs and medicines for the following: diabetes, high

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ARELLANO UNIVERSITY SCHOOL OF LAW BAR OPERATIONS COMMISSION 2025

cholesterol, hypertension, cancer, mental illness, tuberculosis, and kidney diseases. The DOH shall issue a list of medicines for this purpose within 60 days from the effectivity of the TRAIIn Law.

cc. Sale or importation of the following, beginning January 1, 2021 to December 31, 2023:

- i. Capital equipment, its spare parts, and raw materials necessary for the production of personal protective equipment components, such as coveralls, gown, surgical cap, surgical mask, scrub suits, goggles, face shield, double or surgical gloves, and shoe covers, for COVID-19 prevention;
- ii. All drugs, vaccines, and medical devices specifically prescribed and directly used for the treatment of COVID-19; and
- iii. Drugs for the treatment of COVID-19 approved by the Food and Drug Administration (FDA) for use clinical trials, including raw materials directly necessary for the production of such drugs;

Provided, that the Department of Trade and Industry (DTI) shall certify that such equipment, spare parts, or raw materials for importation are not locally available, or are insufficient in quantity, or are not in accordance with the quality specification required;

Provided, further, that for No. 3, the Department of Health (DOH) shall issue a list of prescription drugs and medical devices covered within 60 days from the effectivity of the TRAIN Law and every 3 months thereafter;

Provided, finally, that the exemption claimed under this subsection (BB) shall be subject to post audit by the BIR or the Bureau of Customs, as may be applicable.

dd. Sale or lease of goods or properties or services other than the transactions mentioned in the preceding subsections, the gross annual sales and/or receipts do not exceed P3 million.

In other words, as long as the P3 million VAT threshold is not exceeded, the transaction shall be exempt regardless of its nature. Thus, there would be no need to refer to Section 109(A) to (BB).

The sale of the parking lots is subject to VAT regardless of the amount of the selling price. Parking lots are considered sold separately from the sale of condominium units. Thus, the exemption accorded to sale of residential dwellings for a purchase price not exceeding the exemption threshold does not extend to the parking lots. (*RR. No. 13-2012*)

RR No. 8-2015 restored the VAT exempt status of raw sugar previously withdrawn under the subject RR No. 13-2013. This development constitutes a supervening event which renders the main action for declaratory relief against the constitutionality of the old RR No. 13-2013 academic. It clarified that in cases where the main action has become academic, so have the ancillary relief for TRO or writ of injunction and all related incidents, including petitioners' opposition to its issuance and the present petition to nullify the writ of injunction issued by the trial court. (***Secretary of Finance vs. Munez, G.R. No. 212687, July 20, 2022, Lazaro-Javier, J.***)

ARELLANO UNIVERSITY SCHOOL OF LAW BAR OPERATIONS COMMISSION 2025

g. INPUT AND OUTPUT TAX

Output VAT

This refers to the value-added tax due on the sale or lease of taxable goods or properties or services by any person registered or required to register. (*Sec. 110 (A)(3)(B), NIRC, as amended*)

It is a liability to be paid by the seller of goods and /or services to the BIR. In short, output tax is derived only from sales or transaction deemed sales which are vatatable at 12%.

Input VAT

It pertains to the value-added tax due on or paid by a VAT-registered person in the course of his trade or business on importation of goods or local purchase of goods or services, including lease or use of property, from a VAT-registered person. It shall also include the transitional input tax. (*Sec. 110 (A)(3)(B), NIRC, as amended*)

It also includes input taxes which can be directly attributed to transactions subject to VAT plus a ratable portion of any input tax which cannot be directly attributed to either the taxable or exempt activity.

Sources of Input Tax

Any input tax evidenced by a VAT invoice or official receipt issued in accordance with

Section 113 hereof on the following transactions shall be creditable against the output tax (*Sec. 110, NIRC, as amended*)

1. Purchase or Importation of Goods

- a. For sale; or
- b. For conversion into or intended to form part of a finished product for sale including packaging materials; or
- c. For use as supplies in the course of business; or
- d. For use as materials supplied in the sale of service; or

e. For use in trade or business for which deduction for depreciation or amortization is allowed under this Code.

2. Purchase of real properties for which a VAT has actually been paid;
3. Purchase of services in which VAT has actually been paid;
4. Transactions deemed sale;
5. Presumptive Input Tax;

Persons or firms engaged in the processing of sardines, mackerel and milk, and in manufacturing refined sugar, cooking oil and packed noodle based instant meals, shall be allowed a presumptive input tax, creditable against the output tax, equivalent to four percent (4%) of the gross value in money of their purchases of primary agricultural products which are used as inputs to their production. (*Sec. 111(B), NIRC, as amended*)

'Processing' shall mean pasteurization, canning and activities which through physical or chemical process alter the exterior texture or form or inner substance of a product in such manner as to prepare it for special use to which it could not have been put in its original form or condition.

6. Transitional Input Tax

A person who becomes liable to value added tax or any person who elects to be a VAT-registered person shall, subject to the filing of an inventory, be allowed input tax on his beginning inventory of goods, materials and supplies equivalent to two percent (2%) of the value of such inventory or the actual value-added tax paid on such goods, materials and supplies, whichever is higher, which shall be

ARELLANO UNIVERSITY SCHOOL OF LAW BAR OPERATIONS COMMISSION 2025

creditable against the output tax. (*Sec. 111(A), NIRC, as amended*)

Output VAT on uncollected receivable

Under the Ease of Paying Taxes Act, a seller of goods or services may deduct the output VAT pertaining to uncollected receivables from its output VAT on the next quarter, after the lapse of the agreed upon period to pay: provided, that the seller has fully paid the VAT on the transaction: provided, further, that the VAT component of the uncollected receivables has not been claimed as a bad debt expense. (*Sec. 110(D), NIRC, as amended*)

Uncollected Receivable refers to sales of goods and/ or services on account that transpired upon the effectivity of these Regulations which remain uncollected by the buyer despite the lapse of the agreed period to pay. (*RR No. 3-2024*)

To be entitled to VAT credit, the following requisites must be present:

- a. The sale or exchange has taken place after 27 April 2024;
- b. The sale is on credit or on account;
- c. There is a written agreement on the period to pay the receivable, i.e., credit term is indicated in the invoice or any document showing the credit term;
- d. The VAT is separately shown on the invoice;
- e. The sale is specifically reported in the Summary List of Sales covering the period when the sale was made and not reported as part of "various" sales;
- f. The seller declared in the tax return the corresponding output VAT indicated in the invoice within the period prescribed under existing rules;
- g. The period agreed upon, whether extended or not, has elapsed; and
- h. The VAT component of the uncollected receivable was not claimed as a deduction from gross income (i.e., bad debt). (*RR No. 3-2024*)

In case of recovery of uncollected receivables, the output VAT pertaining thereto shall be added to the output VAT of the taxpayer during the period of recovery. (*Sec. 110(D), NIRC, as amended*)

Claim for Input Tax on Capital Goods

Capital goods or properties - refers to goods or properties with estimated useful life greater than one (1) year and treated as depreciable assets used directly or indirectly in the production or sale of taxable goods or service (*Sec. 4.110-3, RR 16-05 as amended by RR 13-2018*)

1. For capital goods where aggregate acquisition costs exceed PhP 1 Million in one month, regardless of the acquisition cost of each capital good - the input VAT shall be spread evenly over a period of sixty (60) months or useful life, whichever is lower. The claim for input tax credit will commence in the calendar month when the capital good is acquired;
2. If aggregate acquisition cost does not exceed PhP 1 Million in one month - the total input taxes will be allowable as credit against output tax in the month of acquisition.

NOTE: The amortization of the input VAT shall be only allowed until December 31, 2021, after which taxpayers with unutilized input VAT on capital goods purchased or imported shall be allowed to apply the same as scheduled until fully utilized. (*Sec. 110, NIRC, as amended by TRAIN Law*).

If the depreciable capital good is sold/transferred within a period of five (5) years or prior to the exhaustion of the amortizable input tax thereon, the entire unamortized input tax on the capital goods sold/transferred can be claimed as input tax credit during the month/quarter when the sale or transfer was made.

Persons who can avail input tax credits

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ARELLANO UNIVERSITY SCHOOL OF LAW BAR OPERATIONS COMMISSION 2025

The input tax credit on importation of goods or local purchases of goods, properties or services by a VAT-registered person shall be creditable:

1. To the importer upon payment of VAT prior to the release of goods from customs custody;
2. To the purchaser of the domestic goods or properties upon consummation of the sale; or
3. To the purchaser of services or the lessee or licensee upon payment of the compensation, rental, royalty or fee. *(Sec. 4.110-2, RR 16-2005)*

Provided that the invoicing requirements were completely complied with. *(Sec. 113, NIRC, as amended)*.

Non-compliance of the invoicing requirement shall disallow the input tax for crediting regardless if it was purchased from a VAT registered supplier.

VAT Invoicing Requirements

A VAT-registered person shall issue a VAT invoice for every sale, barter, exchange, or lease of goods or properties and for every sale, barter or exchange of services: Provided, That a digital sales or commercial invoice shall be issued for every sale, barter, or exchange of digital services made by a VAT-registered nonresident digital service provider. *(Sec. 113(A), NIRC, as amended)*

The following information shall be indicated in the VAT invoice:

1. A statement that the seller is a VAT-registered person, followed by the seller's Taxpayer's Identification Number;
2. The total amount which the purchaser pays or is obligated to pay to the seller with the indication that such amount includes the value-added tax: Provided, That:

- a. The amount of the tax shall be shown as a separate item in the invoice;
- b. If the sale is exempt from value-added tax, the term VAT-exempt sale shall be written or printed on the invoice;
- c. If the sale is subject to zero percent (0%) value-added tax, the term 'zero-rated sale' shall be written or printed on the invoice.
- d. If the sale involves goods, properties or services some of which are subject to and some of which are VAT zero-rated or VAT exempt, the invoice shall clearly indicate the break-down of the sale price between its taxable, exempt and zero-rated components, and the calculation of the value-added tax on each portion of the sale shall be shown on the invoice: Provided, That the seller may issue separate invoices for the taxable, exempt, and zero-rated components of the sale.

3. The date of transaction, quantity, unit cost and description of the goods or properties or nature of the service; and
4. In the case of sales in the amount of One thousand pesos (P1,000) or more where the sale or transfer is made to a VAT-registered person, the name, address and Taxpayer Identification Number of the purchaser, customer or client.
5. The digital sales or commercial invoice issued by a VAT-registered nonresident digital service provider shall indicate the following information in lieu of the requirements under Section 113, Subsection (b), paragraphs 1 to 4:

- a. Date of the transaction;
- b. Transaction reference number;

DO NOT REPRODUCE

ARELLANO UNIVERSITY SCHOOL OF LAW BAR OPERATIONS COMMISSION 2025

- c. Identification of the consumer;
- d. Brief description of the transaction; and
- e. The total amount with the indication that such amount includes the value-added tax:

Provided, That if the sale of digital services includes some services which are subject to VAT, and some that are VAT zero-rated, or VAT-exempt, the invoice shall clearly indicate the breakdown of the sale price by its taxable, VAT-exempt, and VAT zero-rated components: Provided, further, That the calculation of the value-added tax on each portion of the sale shall be shown on the invoice. *(Sec. 113(B), NIRC, as amended)*

h. TAX REFUND OR TAX CREDIT

Section 110 of the Tax Code provides that if the output VAT exceeds the input VAT at the end of the taxable quarter, the excess shall be paid by the taxpayer. On the other hand, if the input VAT exceeds the output VAT at the end of the taxable quarter, the excess shall be carried over to the succeeding quarter/s.

Grounds

There are only two (2) grounds when a taxpayer may file a claim for refund or credit of input VAT, to wit:

- a. Excess input VAT attributable to zero rated sales *(Sec. 112(A), NIRC, as amended)*
- b. Excess input VAT at the time of cancellation of the VAT registration due to retirement from or cessation of business *(Sec. 112(B), NIRC, as amended)*

Excess input VAT attributable to zero-rated sales may be refunded or credited against other internal revenue taxes, at the option of the VAT-registered person.

A VAT-registered person who is also engaged In transactions not subject to VAT shall be allowed tax credits for the following:

- a. Total input VAT directly attributable to transactions subject to VAT, except sales to the government which are subject to final withholding VAT
- b. Ratable portion of the input VAT which cannot be directly attributed to either activity

Who may claim for refund/credit of excess input tax?

1. Any VAT-registered person, whose sales are zero-rated or effectively zero-rated may, within two (2) years after the close of the taxable quarter when the sales were made, apply for the issuance of a tax credit certificate or refund of creditable input tax due or paid attributable to such sales, except transitional input tax, to the extent that such input tax has not been applied against output tax. *(Sec. 112(A), NIRC, as amended)*

2. A person whose registration has been cancelled due to retirement from or cessation of business, or due to changes in or cessation of status under Section 106(C) of this Code may, within two (2) years from the date of cancellation, apply for the issuance of a tax credit certificate or cash refund for any unused input tax which may be used in payment of his other internal revenue taxes or apply for refund for any unused input tax. *(Sec. 112(B), NIRC, as amended)*

Requirements to Claim Refund or Tax Credit on Unutilized Input VAT for Zero-Rated/Effectively Zero-Rated Sales:

- 1. The taxpayer is VAT-registered;
- 2. The taxpayer is engaged in zero-rated or effectively zero-rated sales;
- 3. The input taxes are due or paid;
- 4. The input taxes are not transitional input taxes;

ARELLANO UNIVERSITY SCHOOL OF LAW BAR OPERATIONS COMMISSION 2025

5. The input taxes have not been applied against output taxes during and in the succeeding quarters;

6. The input taxes claimed are attributable to zero-rated or effectively zero-rated sales;

7. For zero-rated sales under Section 106(A)(2)(a)(1) and (3) and 108(B)(1) and (2), the acceptable foreign currency exchange proceeds have been duly accounted for in accordance with the rules and regulations of the BSP;

8. Where there are both zero-rated or effectively zero-rated sales and taxable or exempt sales, and the input taxes cannot be directly and entirely attributable to any of these sales, the input taxes shall be proportionately allocated on the basis of sales volumes; and

9. The claim is filed within 2 years after the close of the taxable quarter when such sales were made.

(Luzon Hydro Corporation vs. Commissioner of Internal Revenue, G.R. No. 188260, November 13, 2023; Sec. 4.112-1, RR No. 16-2005)

Documentary Requirement on VAT Refund

EOPT Act mandates a single document for both sales of goods and services. Hence, a VAT Invoice shall be issued as evidence of sale of goods and/or properties and sale of services and/or leasing of properties issued to customers in the ordinary course of trade or business, whether cash sales or on account (credit), which shall be the basis of the output tax liability of the seller and the input tax claim of the buyer. *(R.R. No. 7-2024)*

Period to file claim

I. Administrative claim

Application for refund or tax credit certificate shall be filed within 2 years after the close of the taxable quarter when the sales were made, or within 2 years from the date of cancellation

of VAT registration, as the case may be. *(Sec. 112(A)(B), NIRC, as amended)*

In proper cases, the CIR shall grant the refund within 90 days from the date of submission of the official receipts or invoices and other documents in support of the application. Should the CIR find that the grant of refund is not proper, the CIR must state in writing the legal and factual basis for the denial. *(Sec. 112(C), NIRC, as amended)*

II. Judicial Claim

In case of full or partial denial of the claim, the taxpayer affected may, within 30 days from the receipt of the decision denying the claim, appeal the decision with the Court of Tax Appeals. *(Sec. 20, EOPT Law)*

In summary, the following are the crucial periods to remember in filing a claim for input VAT refund or tax credit certificate:

Period	Nature
2 YEARS	<p>This period is reckoned from the close of the taxable quarter when the sales were made, or from the date of cancellation of VAT registration. It applies only to the administrative claim.</p> <p>A judicial claim filed beyond the two-year statutory period is not legally infirm, as long as it is taken within 30 days from the receipt of the denial of the administrative claim.</p> <p>All that is required under the law is that the appeal to the Court of Tax Appeals be made within such 30 days. The judicial claim need not fall within the 2-year period.</p>

ARELLANO UNIVERSITY SCHOOL OF LAW BAR OPERATIONS COMMISSION 2025

Period	Nature
90+30 DAY RULE	<p>The 90 days pertain to the period within which the BIR is required to act on the administrative claim.</p> <p>On the other hand, the 30 days refer to the period within which a judicial appeal can be filed in case of denial of the administrative claim.</p> <p>As a general rule, the 30-day period to appeal is both mandatory and jurisdictional.</p>

Premature Claims

A judicial claim or appeal filed before the lapse of the 120-day (now 90-day) period without a decision or action of the CIR is premature. It shall be dismissed for lack of jurisdiction. (*Aichi Forging Company of Asia, Inc. vs. CTA En Banc*, G.R. No. 193625, August 30, 2017)

This 120-day (now 90-day) period is both mandatory and jurisdictional, such that the taxpayer is forced to await the expiration of the period before initiating an appeal before the Court of Tax Appeals. This must be so because prior to the expiration of this period, the CIR still has the statutory authority to render a decision. If there is no decision and the period has not yet expired, there is nothing to contest in the meantime. (*Ibid.*)

Otherwise stated, there is no cause of action yet that would justify resort to the court. Premature invocation of the court's jurisdiction is fatally defective and is susceptible to dismissal. (*Ibid.*)

Exception:

BIR Ruling No. DA-489-03 excused premature filing by declaring that the taxpayer-claimant need not wait for the lapse of the 120 days (now 90 days). Consequently, while this Ruling

was in force from December 10, 2003 until it was declared invalid by the Supreme Court under the Aichi ruling which was promulgated on October 6, 2010, premature judicial claims shall not be dismissed to the prejudice of the taxpayer. (*CIR vs. Achi Forging Company Asia, Inc.*, G.R. No. 184823, October 6, 2010)

BIR Ruling No. DA-489-03, which expressly allowed the filing of judicial claims with the Court of Tax Appeals even before the lapse of the 120-day (now 90-day) period, provided for a valid claim of equitable estoppel because the CIR had misled taxpayers into prematurely filing their judicial claims before the Court of Tax Appeals. (*Sitel Philippines Corporation vs. CIR*, G.R. No. 201326, February 8, 2017)

Belated Claims

A judicial claim filed beyond 30 days from the receipt of the CIR's decision or from the 90th day of inaction by the CIR shall be barred by prescription.

BIR Ruling No. DA-489-03, which created an exception to the mandatory and jurisdictional nature of the 120 (now 90)+30-day rule, does not cover claims belatedly filed. It covers only premature judicial claims. (*Steag State Power vs. CIR*, G.R. No. 205282, January 14, 2019)

San Roque Doctrine

In a claim for refund or credit of "excess" input VAT under Sec. 110(B) (Tax Credits) and Sec. 112(A) (Refunds or Tax Credits of Input Tax), the input VAT is not "excessively" collected as understood under Sec. 229. At the time of payment of the input VAT the amount paid is the correct and proper amount. Under the VAT System, there is no claim or issue that the input VAT is "excessively" collected, that is, that the input VAT paid is more than what is legally due. The person legally liable for the input VAT cannot claim that he overpaid the input VAT by the mere existence of an "excess" input VAT.

The term "excess" input VAT simply means that the input VAT available as credit exceeds the output VAT, not that the input VAT is excessively collected because it is more than

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ARELLANO UNIVERSITY SCHOOL OF LAW BAR OPERATIONS COMMISSION 2025

what is legally due. Thus, the taxpayer who legally paid the input VAT cannot claim for refund or credit of the input VAT as "excessively" collected under Section 229. (*CIR vs. San Roque Power Corporation*, G.R. No. 187485, February 12, 2013)

A claim for tax refund or credit, like a claim for tax exemption, is construed strictly against the taxpayer. One of the conditions for a judicial claim of refund or credit under the VAT System is compliance with the 120 (now, 90) + 30 day mandatory and jurisdictional periods. Thus, strict compliance with the 120 (now, 90)+30 day period is necessary for such a claim to prosper, whether before, during, or after the effectivity of the Atlas doctrine, except for the period from the issuance of BIR Ruling No. DA-489-03 on 10 December 2003 to 6 October 2010 when the Aichi doctrine was adopted, which again reinstated the 120(now, 90)+30 day period as mandatory and jurisdictional (*CIR vs. San Roque Power Corporation/Taganito Mining Corporation vs. Commissioner of Internal Revenue* G.R. 187485, October 8, 2013; *Steag State Power vs. CIR*, G.R. No. 205282, January 14, 2019)

The post facto denial of Taihei's administrative claims is irrelevant as CIR's inaction for 120 (now, 90) days is already considered "deemed denial" of the administrative claims for refund. Without a timely appeal, the "deemed denial" becomes final and unappealable. One of the conditions for filing a judicial claim of refund or credit under the VAT System is adherence to the mandatory and jurisdictional 120(now, 90-day)+30-day periods. Thus, strict compliance with the 120 (now, 90-day)+30-day periods is necessary for such a claim to prosper. Here, Taihei was clearly negligent when it failed to file its judicial claims after the lapse of the 120(now, 90)-day period and within the 30-day window. (***Taihei Alltech Construction vs. CIR*, G.R. No. 258791, 07 December 2022, Lazaro-Javier, J)**

The input tax attributable to zero-rated sales may, at the option of the VAT-registered taxpayer, be: (1) charged against output tax

from regular 12% VAT-able sales, and any unutilized or "excess" input tax may be claimed for refund or the issuance of tax credit certificate; or (2) claimed for refund or tax credit in its entirety. (*Chevron Holding, Inc. vs. CIR*, G.R. No. 215159, July 05, 2022)

It must be stressed that the remedies of charging the input tax against the output tax and applying for a refund or tax credit are alternative and cumulative. Furthermore, the option is vested with the taxpayer-claimant. In such case, the taxpayer only needs to prove

non-application or non-charging of the input-VAT subject of the claim. There is nothing in the law and rules that mandate the taxpayer to deduct the input tax attributable to zero-rated sales from the output tax from regular twelve percent (12%) VAT-able sales first and only the "excess" may be refunded or issued a tax credit certificate. (*Ibid.*)

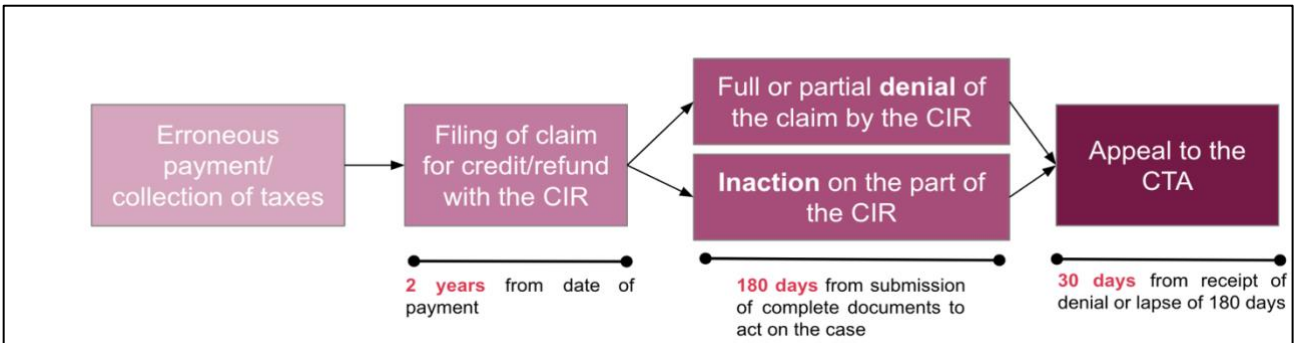
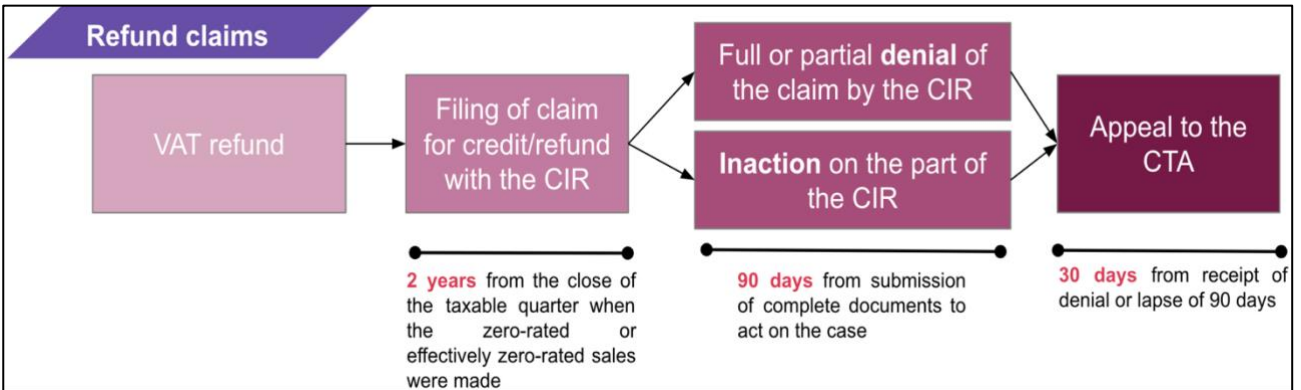
Effect of Failure to Print "Zero-Rated" on Sales Invoices or Receipts to Claim for Refund or Credit

If the claim for refund/TCC is based on the existence of zero-rated sales by the taxpayer but it fails to comply with the invoicing requirements in the issuance of sales invoices (e.g., failure to indicate the TIN), its claim for tax credit/refund of VAT on its purchases shall be denied considering that the invoice it is issuing to its customers does not depict its being a VAT-registered taxpayer whose sales are classified as zero-rated sales. The appearance of the word "zero-rated" on the face of invoices covering zero-rated sales prevents buyers from falsely claiming input VAT from their purchases when no VAT was actually paid. If, absent such word, a successful claim for input VAT is made, the government would be refunding money it did not collect. Thus, the absence of the word "zero-rated" on its invoices is a proper ground for denial of a claim for refund. (*Panasonic Communications Imaging Corporation of the Philippines vs. Commissioner of Internal Revenue*, G.R. No. 178090, February 8, 2010)

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Refund claims under EOPT Law



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3. TAX REMEDIES

a. General Concepts

It refers to procedural steps that may be undertaken by the government or a taxpayer for the resolution of disputes concerning the levy or imposition, assessment, collection, and refund of taxes (*DOMONDON, Taxation, Tax Remedies 2014*).

On the part of the Government	On the part of the Taxpayer
Courses of action provided by or allowed in the law to implement the tax laws or enforce tax collection.	Legal actions which a taxpayer can avail of to seek relief from the undue burden or oppressive effect of tax laws, or as a means to check possible excesses by revenue officers in the performance of their duties.

i. Tax Deficiency vs Tax Delinquency

Distinguish Tax Deficiency vs Tax Delinquency

Tax Deficiency	Tax Delinquency
Amount still due and collectible from a taxpayer upon audit or investigation.	failure of the taxpayer to pay the tax due on the date fixed by law or indicated in the assessment notice or letter of demand.
Amount by which the tax imposed or required to be paid exceeds the tax actually paid and shown in the taxpayer's return. If the taxpayer disagrees with the assessment for tax deficiency, he must file a protest with the BIR (administrative	Arises when the taxpayer's protest against a disputed assessment has already been denied by the Commissioner in whole or in part, and the deficiency tax assessment has become final, executory and demandable. A delinquent tax can be

Tax Deficiency	Tax Delinquency
appeal) and in case of denial, an appeal to the Court of Tax Appeals (judicial remedies)	immediately collected administratively through distraint or levy.

(Takenaka Corporation Philippine Branch v. CIR, CTA EB No. 745, Sept. 4, 2012)

Tax Deficiency	Tax Delinquency
Availability	
Exists when: (1) the self-assessed tax is not paid at all or was only partially paid on the prescribed date, or (2) when the deficiency tax assessed by the BIR has become final and executory	Exists when: the amount imposed by law (as determined by CIR or his authorized representative) exceeds amount shown as tax upon taxpayer's return NOTE: <i>An amount is determined by the BIR as a tax liability where there is no amount stated in the return</i>
Collection Process	
Can be immediately collected	To be collected, has to go through the assessment process.
Remedy	
Filing of a civil action for the collection of taxes is the proper remedy	Filing of a civil action during pendency of protest is a ground for a motion to dismiss
Penalties	
Is subject to surcharges and administrative penalties.	Subject to 25% surcharge, although subject to interest and compromise penalty.

ii. Tax Evasion

[See discussions under Part A.8.c. Tax Evasion]

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b. Civil Penalties

(i) Deficiency Interest and Delinquency Interest

Definition of Deficiency Interest

Imposed on any deficiency tax due, which will be assessed and collected from the date prescribed for payment until the full payment or upon the issuance of a notice of demand by the BIR, whichever comes first. (*Section 249 (B), NIRC*)

Definition of Delinquency Interest

Imposed on the failure to pay the amount of tax due on any return to be filed, the amount of tax due for which no return is required, or deficiency tax or any surcharge or interest appearing in the notice of demand. (*Section 249 (C), NIRC*)

Rule on double imposition of deficiency interest and delinquency interest

No double imposition of interest pursuant to TRAIn Law. There shall be assessed and collected on any unpaid amount of tax, interest at the rate of double the legal interest rate for loans or forbearance of any money in the absence of an express stipulation as set by the BSP from the date prescribed for payment until the amount is fully paid. Provided, that in no case shall the deficiency and the delinquency interest prescribed be imposed simultaneously. (*Sec. 249(A), NIRC*)

Deficiency and delinquency interests cannot be imposed simultaneously. The interest rate prescribed for deficiency tax and delinquent tax liabilities is twelve percent (12%), which is twice the prevailing interest rate of six percent (6%) from the BSP. (*RR No. 21-2018*)

Distinguish Deficiency Interest and Delinquency Interest

Deficiency Interest	Delinquency Interest
Amount still due and collectible from a taxpayer upon audit or investigation	Failure to pay the tax due on the date fixed by law or indicated in the assessment notice or letter of demand
Shortage of taxes paid	Delay in payment of taxes
Tax Base	
Basic Tax	Basic tax plus interest and surcharges
Reckoning Point	
From the date prescribed until the full payment or upon issuance of notice and demand by the CIR, whichever is earlier	From the date appearing in the notice and demand by the CIR
Rate	
12% (2x the legal rate set by BSP)	12% (2x the legal rate set by BSP)

(ii) Surcharge

Surcharge is the civil penalty for the delay in the payment of the taxes due.

The rates of surcharge are as follows:

- 25% of the amount due in the following cases:
 - (1) Failure to file any return and pay the tax due thereon as required by the Code or rules and regulations on the date prescribed;
 - (2) Failure to pay deficiency tax within the time prescribed for its payment in the notice of assessment;
 - (3) Failure to pay full or part of the amount of tax shown on any return required to be filed under the provisions of the NIRC or rules or regulations or the full amount of tax due thereon for which no return is required to be filed, on or before the date prescribed for its payment. (*Section 248(a), NIRC*).

ARELLANO UNIVERSITY SCHOOL OF LAW BAR OPERATIONS COMMISSION 2025

NOTE: The EOPT law deleted **the civil penalty of twenty-five percent (25%) in case of filing a return with an internal revenue officer other than those with whom the return is required to be filed.**

There are no longer any penalties imposed on filing a return at the wrong venue. Should the taxpayer be considered as micro or small taxpayer, the surcharge shall be ten percent (10%). (*Section 41, EOPT Law*)

b. 50% of the tax or of the deficiency tax in case any payment has been made, in the following cases:

1. In case of willful neglect to file return within the period prescribed by the NIRC or by rules and regulations; and
2. In case fraudulent return is willfully made.

Provided, that substantial underdeclaration of sales or substantial overstatement of deductions, as determined by CIR, shall constitute prima facie evidence of a false or fraudulent return. Provided, further, that failure to report sales in an amount exceeding 30% of that declared per return, and a claim of deductions in an amount exceeding 30% of actual deductions, shall render the taxpayer liable for substantial underdeclaration of sales or for overstatement of deductions. (*Section 248(b), NIRC*)

The payment of surcharge is **mandatory** and the BIR is not vested with any authority to waive or dispense with the collection thereof. (*Philex vs. CIR, G.R. No. 125704, August 28, 1998*)

Surcharge imposed due to one day late filing is not unjust or excessive. The law itself provides for the imposition of a penalty equivalent to 25% of the amount due for failure to timely file any return and pay the tax due thereon. *Dura lex sed lex. (Qatar Airways Company with Limited Liability vs CIR, G.R. No. 238914, June 08, 2020)*

(iii) Compromise Penalty

A compromise penalty is an amount of money paid by a taxpayer to compromise a tax violation that he has committed, instead of the BIR instituting a criminal action against the taxpayer. A compromise is consensual in character, hence, may not be imposed on the taxpayer without his consent (*RR No. 12-1999*).

Compromise penalties are amounts collected in lieu of criminal prosecution for violations committed by the taxpayer, where the payment is based on a compromise agreement validly entered between the taxpayer and the Commissioner of Internal Revenue. Although all amounts of compromise penalties incident to violations shall be itemized in the assessment notice and/or demand letter, the same should not form part of the assessment notice that reflects deficiency basic tax, surcharge, and interest but should appear in a separate assessment notice and/or demand letter as the amount suggested to the taxpayer to pay in lieu of criminal prosecution. (*RMC No. 3-2022*)

A compromise implies agreement. One party cannot impose it upon the other. If an offer of compromise is rejected by the taxpayer, the Commissioner of Internal Revenue should file a criminal action if he believes that the taxpayer is criminally liable for the violation of the tax law as the only way to enforce a penalty. A penalty can be imposed only on a finding of criminal liability. (*CIR vs Abad, G.R. No. L-19627, June 27, 1968*)

All criminal violations may be compromised except: (a) Those already filed in court; or (b) Those involving fraud. (*Section 204 (B), NIRC*)

Covered Persons

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Covered Person	Amount
Any person required by the Code and rules and regulation and willfully fails to (1) pay any tax, (2) make such return, (3) keep such record, or (4) supply correct and accurate information, (5) withhold or remit taxes withheld, or (6) refund excess taxes withheld on compensation, at the time or times required.	A fine of not less than P10,000 and suffer imprisonment of not less than 1 year but not more than 10 years, in addition to other penalties provided by law.
Any person who attempts to (1) make it appear that he has filed a return or statement, or (2) actually files a return or statement and subsequently withdraws the same return or statement after securing the official receiving seal or stamp of receipt of the internal revenue office wherein the same was actually filed.	Upon conviction, a fine of not less than P10,000 but not more than P20,000 and suffer imprisonment of not less than 1 year but not more than three 3 years.

c. Assessment Process

Definition

Tax assessment is the act of an authorized official ascertaining the amount of tax due from the taxpayer. It is what triggers the tax remedies process. *[Basic Taxation Law: Including the Ease of Paying Act (EOPT), p. 301, 2024 edition]*

It refers to procedural steps that may be undertaken by the government or a taxpayer for the resolution of disputes concerning the levy or imposition, assessment, collection, and refund of taxes. *(DOMONDON, Taxation, Tax Remedies 2014)*

An **assessment** refers to the determination of amounts due from a person obligated to make payments. In the context of national internal revenue collection, it refers to the determination of the taxes due from a taxpayer under the 1997 NIRC, as amended.

The assessment process starts with the filing of tax return and payment of tax by the taxpayer. The initial assessment evidenced by the tax return is a self-assessment of the taxpayer. The tax is primarily computed and voluntarily paid by the taxpayer without need of any demand from government. If tax obligations are properly paid, the Bureau of Internal Revenue (BIR) may dispense with its own assessment.

Tax collection must be preceded by a valid assessment to allow the taxpayer to protest the assessment, present their case and adduce supporting evidence. Without complying with the unequivocal mandate of first informing the taxpayer of the government's claim, there can be no deprivation of property, because no effective protest can be made. *(CIR vs. Unioil Corporation, G.R. No. 204405, August 04, 2021)*

After filing a return, the Commissioner or his or her representative may allow the examination of any taxpayer for assessment of proper tax liability. *(CIR vs. Izone Technologies Philippines, CTA EB Case No. 2295, May 05, 2022, citing Commissioner vs. Fitness by Design, G.R. No. 215957, November 09, 2016).*

An assessment, however, is not altogether inconsequential; it is relevant in the proper pursuit of judicial and extra judicial remedies to enforce taxpayer liabilities and certain matters that to enforce taxpayer liabilities and certain matters that relate to it, such as the imposition of surcharges and interest, and in the application of statutes of limitations and establishment of tax liens. *(Tupaz v. Ulep, G.R. 127777, October 1, 1999)*

A jeopardy assessment is a tax assessment without the benefit of a complete or partial audit by an authorized revenue officer, who has

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reason to believe that the collection of a deficiency tax will be jeopardized by delay because of the taxpayer's failure to comply with the audit and investigation requirements to present books of accounts and/or pertinent records, or to substantiate all or any of the deductions, exemptions, or credits claimed in the tax return. (*RR No. 30-2002*)

NOTE: Concept of assessments: As the above jurisprudence mentions, the filing of tax returns is voluntary and self – assessing, meaning it is up to the taxpayer whether to file their own taxes and what amount will be reported in the tax returns. BIR, in turn, has the vital role of checking whether the amounts reported by the taxpayer is correct through an audit which is initiated through a BIR document called **Letter of Authority (LOA)**. Any findings made shall be communicated to the taxpayer by way of an **Assessment**. The taxpayer in turn by way of due process responds through filing of **protest**. (*Id.*)

Requisite of a Valid Assessment

1. The assessment must be in writing and signed by the Commissioner or his duly authorized representative (*Section 228, NIRC, as amended*)
2. It must contain a computation of tax liabilities, demand for payment and definite due date (*CIR v. Fitness by Design Inc., G.R. No. 215957, November 09, 2016*)
3. It must state the factual and legal bases of the assessment on which it is based (*Section 226, NIRC, as amended*)
4. It must be issued on account of or covered by a validly issued Letter of Authority (LOA) (*CIR v. Sony Philippines, G.R. No. 178697, November 17, 2010*)
5. It must be issued within the Original prescriptive period prescribed by law or within the extended prescriptive period as validly agreed between the BIR and the taxpayer (*Sections 203 & 222, NIRC*);

6. It must be served on and received by the taxpayer (*CIR v. Pascor Realty & Development Corporation et. al., G.R. No. 128315, June 29, 1999*)

Procedural Due Process in Tax Assessment

1. Issuance of a LOA;
2. Tax Audit or Investigation;
3. Issuance of Notice of Discrepancy (NOD) (*RR No. 22-2020*)
4. Issuance of Preliminary Assessment Notice (PAN);
5. Protest or If no protest, taxpayer considered as default;
6. Issuance of Final Assessment Notice (FAN) or Formal Letter of Demand (FLD); and
7. Filing of Administrative action (i.e., Request for reconsideration or for reinvestigation/ Inaction on Disputed
8. Issuance of Final Decision on Disputed Assessment (FDDA)
9. Filing of Judicial Protest (i.e., appeal to the CTA)

Letters and Notices shall be issued to the taxpayer to comply with the right to due process of a taxpayer:

1. Letter of Authority (LOA);
2. Notice of Discrepancy (NOD);
3. Preliminary Assessment Notice (PAN);
4. Formal Letter of Demand and Final Assessment Notice (FLD/FAN);
5. Final Decision on Disputed Assessment (FDDA)

NOTE: Absence of any of the foregoing can be used by the taxpayer to dispute the deficiency tax assessment on the ground of violation of the right to due process.

i. Letter of Authority

A LOA refers to a letter informing a taxpayer that a certain revenue officer is authorized to examine the books of accounts and other accounting records of said taxpayer for the purpose of verifying his tax liabilities during a taxable year.

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It commences the audit process and informs the taxpayer that it is under audit for possible deficiency tax assessment. (*CIR vs. De La Salle University, Inc. GR No. 196596, Nov. 9, 2016*)

A LOA would include the following information: (1) taxes covered; (2) period covered; (3) authorized examiners; and (4) authorized signatory.

There must be a grant of authority before any revenue officer (RO) can conduct an examination or issue an assessment. In the absence of such an authority, the assessment or examination is a nullity. Thus, the BIR cannot extend its examination or assessment beyond the period covered by the LOA. The LOA **should cover a taxable period not exceeding one taxable year**. The practice of issuing an LOA covering audit of "unverified prior years" is prohibited. (*CIR vs. Sony Philippines, Inc. G.R. No. 178797, 17 November 2010*)

A LOA is premised on the fact that the examination of a taxpayer who has already filed his tax returns is a power that statutorily belongs only to the CIR himself or his duly authorized representatives.

In the absence of such an authority, the assessment or examination is a nullity. (*Medicard Philippines, Inc. v. CIR, G.R. No. 222743, April 5, 2017*)

Prohibition on amendment of returns once LOA is served

Any return, statement of declaration filed in any office authorized to receive the same shall not be withdrawn. Provided, that within three (3) years from the date of such filing, the same may be modified, changed, or amended. Provided, further, that no notice for audit or investigation of such return, statement or declaration has in the meantime been actually served upon the taxpayer. (*Section 6(a), NIRC*)

Absence of a LOA makes the revenue officer's examination of the books of the taxpayer unauthorized

The Commissioner or his duly authorized representative may authorize the examination of any taxpayer and the assessment of the correct amount of the tax. It is thus a necessity to issue the LOA in order to authorize the LOA in order to authorize the examiners to conduct an audit/examination of the books of the taxpayer. (*Section 6(A), NIRC*)

After a tax return has been filed, the BIR is authorized to examine the taxpayer and assess the correct amount of tax. However, the failure of the taxpayer to file a return shall not prevent the BIR from examining the taxpayer. (*Section 6(A) & Section 13, NIRC*)

A LOA is premised on the fact that the examination of a taxpayer who has already filed his tax returns is **a power that statutorily belongs only to the CIR** himself or his duly authorized representatives. In the absence of such an authority, **the assessment or examination is a nullity.** (*Medicard Philippines, Inc. v. CIR, G.R. No. 222743, April 5, 2017*)

Examination of Books of Account

General rule: The books of account shall be subject to examination and inspection only once every taxable year. (*Section 235, NIRC*)

Exceptions:

1. Fraud, irregularity or mistakes, as determined by the Commissioner;
2. The taxpayer requests for reinvestigation;
3. Verification of compliance with withholding tax laws and regulations;
4. Verification of capital gains tax liabilities; and
5. In the exercise of the Commissioner's power under Section 5(B) to obtain information from
6. Other persons in which case, another or separate examination and inspection may be made.

ARELLANO UNIVERSITY SCHOOL OF LAW BAR OPERATIONS COMMISSION 2025

Requisites of a valid LOA

1. It must be issued by the **Proper approving official**
 - a. Regional Director (RD) – in cases of LOA made by Regional District Offices (RDO)
 - b. Assistant Commissioner – Large Taxpayer Services (ACIR – LTS) and its divisions
 - c. Deputy Commissioner Legal and Inspection Group – Enforcement Services and
 - d. CIR or any authorized official – Task Force and Special Teams
2. It must not contain any manually – written character, notation or **Erasure**;
3. Must cover **only one (1) Taxable year**, except in tax fraud cases authorized by the CIR or Deputy Commissioner and excise taxes;

If the audit of a taxpayer shall include more than one taxable period, the other periods or years shall be specifically indicated in the LOA. The requirement to specify the taxable period covered by the LOA is simply to inform the taxpayer of the extent of the audit and the scope of the revenue officer's authority. Without this rule, a revenue officer can unduly burden the taxpayer by demanding random accounting records from random unverified years, which may include documents from as far back as ten years in cases of fraud audit (*CIR vs. De La Salle University, Inc., G.R. No. 196596, November 9, 2016*).

4. Must indicate **the Taxes covered** by the LOA;
5. Must indicate the names of **Authorized** BIR officers to audit said entity; (*RMO 44-2010 and RMC 82-2022*)

Issuance of the LOA within 30 days is no longer required

The requirement for the BIR to serve the LoA to the taxpayer within 30 days from issuance has been removed. The deletion of this requirement shall not be an excuse for the concerned RO to delay its service nor for a taxpayer to refuse its service or to question its validity, in case the same is served beyond the 30-day period. What is crucial is that the entire audit process shall be completed within a period of 180 days for RDO cases and 240 days for LT cases from the date of issuance of the LOA. (*RMC No. 82-2022*)

Revalidation of the LOA

A revalidation of an expired LOA shall require the issuance of a new LOA, with the corresponding notation thereto, including the previous LOA number and date of issue of said LOAs. (*Dakay Construction & Development Corporation vs. CIR, CTA EB No. 1294, 20 September 2016*)

Reassignment of the LOA

The practice of reassigning or transferring revenue officers originally named in the LOA and substituting or replacing them with new revenue officers to continue the audit or investigation without a separate or amended LOA (i) violates the taxpayer's right to due process in a tax audit or investigation; ii) usurps the statutory power of the Commissioner of Internal Revenue (CIR) or his duly authorized representative to grant the power to examine the books of account of a taxpayer; and i) does not comply with existing Bureau of Internal Revenue (BIR) rules and regulations on the requirement of an LOA in the grant of authority by the CIR or his duly authorized representative to examine the taxpayer's books of accounts. (*CIR vs. McDonald's Philippines Realty Corporation, G.R. No. 242670, May 10, 2021*)

The lack of authority of the revenue officers is tantamount to the absence of a LOA itself which results in a void assessment. (*Himlayang Pilipino Plans, Inc. vs CIR, G.R. No. 241848, May 14, 2021*)

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The necessity of a validly issued LOA for the valid conduct of a taxpayer investigation by an RO is a well-settled doctrine embodied in our statutory and case law. Any re-assignment/transfer of cases to another RO(s), and revalidation of LOAs that have already expired, shall require the issuance of a new LOA. (*Republic of the Philippines vs. Robiegie Corporation, G.R. No. 260261, October 3, 2022*)

Cases which need not be covered by a valid LOA:

1. Cases involving civil or criminal tax fraud which fall under the jurisdiction of the tax fraud division of the Enforcement Services; and
2. Policy cases under audit by the Special Teams in the National Office. (*RMO 36-99*)

Distinguish LOA from Letter Notice

Letter of Authority	Letter Notice
Purpose	
A LOA addressed to a revenue officer is required under the Tax Code before an examination of a taxpayer may be had	An LN is not found in the Tax Code and is only for the purpose of notifying the taxpayer that a discrepancy is found based on the BIR's Reconciliation of Listings for Enforcement (RELIEF) System

ii. Submission of Supporting Documents by Taxpayer

Upon receipt of the LOA, the taxpayer will receive a checklist of documents that the BIR will require the taxpayer to submit in connection with the audit.

The submission of supporting documents allows taxpayers to substantiate their claims, refute findings, and clarify details in cases where the BIR has identified potential tax deficiencies or other issues. This remedy is available at various stages of the tax assessment process, from the preliminary stages to appeals.

That supporting the relevant documents mentioned in the law refers to such documents which the taxpayer feels would be necessary to support his protest and not what the Commissioner feels should be submitted, otherwise, taxpayer would always be at the mercy of the BIR which may require production of such documents which taxpayer could not produce. (*Standard Chartered Bank vs. CIR, CTA Case No. 5696, August 16, 2001*)

Supporting documents may include receipts, vouchers, invoices, contracts, bank statements, financial records, affidavits, and other documentation that substantiates the taxpayer's claims or refutes the BIR's findings.

Notices	Validity
First Notice	After 10 days from receipt of the checklist and the taxpayer did not comply, a First Notice will be sent to the taxpayer.
Second and Final Notice	After 10 days from receipt of the First Notice and the taxpayer still did not comply, a Second and Final Notice will be sent to the taxpayer.
Subpoena Duces Tecum (SDT)	After 10 days from receipt of the Second and Final Notice and the taxpayer still did not comply, the authorized BIR officer shall request for the issuance of a subpoena from the Assistant Commissioner, Enforcement and Advocacy Service (National Office) or Assistant Commissioner, Large Taxpayers Service (Large Taxpayers Service) or Revenue Regional Directors (Regional Office) (<i>RMO No. 45-2010</i>)

ARELLANO UNIVERSITY SCHOOL OF LAW BAR OPERATIONS COMMISSION 2025

Notices	Validity
	In case the taxpayer refuses to comply with the SDT, the concerned BIR legal office shall file a criminal case against the taxpayer for violation of Sec 5 in relation to Secs. 14 and 266 of the NIRC and/or initiate a proceeding to cite the taxpayer for contempt. <i>(RMO No. 10-2013)</i>

Jeopardy Assessment

A "Jeopardy Assessment" is one made without the benefit of complete or partial audit by an authorized revenue officer, who has reason to believe that the assessment and collection of a deficiency tax will be jeopardized by delay because of the taxpayer's failure to comply with the audit and investigation requirements to present his books of accounts and/or pertinent records, or to substantiate all or any of the deductions, exemptions, or credits claimed in his return *(Section 3 (1)(a), RR No. 30-2002, RMC No. 34-2014)*

This is issued basically to comply with the prescriptive period and to prevent the same from lapsing principally from the taxpayer's fault. The Revenue Officer would usually cause the issuance of a subpoena duces tecum to ensure submission of books of accounts, records and/or documents. *(Id)*

iii. Notice of Discrepancy

If a taxpayer is found to be liable for deficiency tax or taxes in the course of an investigation conducted by a Revenue Officer, the taxpayer shall be informed through a Notice of Discrepancy.

If the taxpayer disagrees with the discrepancy/ies detected during the audit, they must explain and provide documents. The documents are submitted within 30 days after receipt of the NOD.

The Revenue Officer who audited the taxpayer's records shall, among others, state in the initial report of investigation of his findings of discrepancies. *(RR No. 7-2018 as amended by RR No. 22-2020)*

Requisites of Notice of Discrepancy

1. Must be based on the Revenue Officer's submitted initial report of investigation;
2. The taxpayer shall be informed, in writing;
3. Notice is issued by:
 - a. the Revenue District Office or by the Assessment Division/Regional Investigation Division, as the case may be (in the case of Revenue Regional Offices); or
 - b. by the Chief of Division concerned (in the case of the BIR National Office) of the discrepancy or discrepancies in the taxpayer's payment of his internal revenue taxes, for the purpose of the "Discussion of Discrepancy".

Discussion of Discrepancy

The Discussion of Discrepancy shall in no case extend beyond **thirty (30) days from receipt of the Notice of Discrepancy.**

It is during the Discussion of Discrepancy that the taxpayer is given the opportunity to present his side of the case and explain the discrepancy found during the investigation of the Revenue Officer assigned and submit documents to support the explanation or arguments.

The taxpayer must present an explanation and provide documents during the discussion to support his explanation.

Should the taxpayer need more time to present the documents, he/she may submit such documents after the discussion, which should be within thirty (30) days after receipt of the Notice of Discrepancy. *(Id.)*

Effect of Discrepancy Discussion

The investigating office shall endorse the case to the reviewing office and approving official in

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the National Office or the Revenue Regional Office, for issuance of a Deficiency Tax Assessment in the form of a PAN within ten (10) days from the conclusion of the discussion if after being afforded the opportunity to present his side through the Discussion of Discrepancy, and:

a. it is still found that the taxpayer is still liable for deficiency tax or taxes;
AND

b. the taxpayer does not address the discrepancy through payment of the deficiency taxes or the taxpayer does not agree with the findings,

iv. Issuance of Preliminary Assessment Notice (PAN)

If after being afforded the opportunity to present his side through the Discussion of Discrepancy, it is still found that the taxpayer is still liable for deficiency tax or taxes and the taxpayer does not address the discrepancy through payment of the deficiency taxes or the taxpayer does not agree with the findings, the investigating office, shall endorse the case for issuance of PAN within ten (10) days from the conclusion of the Discussion. *(RR No. 12-1999 as amended by RR No. 22-2020)*

Definition of PAN

The PAN is a communication issued by the Regional Assessment Division or any other concerned BIR office, informing a taxpayer who has been audited of the findings of the revenue officer, following the review of these findings.

When the CIR or their duly authorized representative finds that proper taxes should be assessed, they shall first notify the taxpayer of their findings. *(Section 228, NIRC, as amended)*

If after review and evaluation by the CIR or their duly authorized representative, it is determined that there exists sufficient basis to assess the taxpayer for any deficiency tax, a

PAN shall be issued for the proposed assessment. *(RR No. 18-2013)*

Requisites of a Valid PAN

1. In writing and signed by the BIR; and
2. Should inform the taxpayer of the law and the facts on which the assessment is made. *(Section 228, NIRC, as amended)*

Due Process in the Issuance of PAN

General rule: The sending of the PAN to a taxpayer is part of the due process requirement in the issuance of a deficiency tax assessment.

Exceptions to Issuance of PAN

- a. When the finding for any deficiency tax is the result of **MATHEMATICAL ERROR** in the computation of the tax as appearing on the face of the return; or
- b. When the **EXCISE TAX** due on excisable articles has not been paid; or
- c. When a discrepancy has been determined between the **TAX WITHHELD** and the amount **ACTUALLY REMITTED** by the withholding agent; or
- d. When an article locally purchased or imported by an **EXEMPT PERSON**, such as, but not limited to, vehicles, capital equipment, machineries and spare parts, has been sold, traded or transferred to a non-exempt person; or
- e. When a taxpayer who opted to claim a refund or tax credit of excess creditable withholding tax for a taxable period was determined to have **CARRIED OVER** and automatically applied the same amount claimed against the estimated tax liabilities for the taxable quarter or quarters of the succeeding taxable year. *(Section 228, NIRC)*

In the above-cited cases, a FLD/FAN shall be issued outright. *(RR No. 18-13)*

The taxpayer must first be informed that he is liable for deficiency taxes

ARELLANO UNIVERSITY SCHOOL OF LAW BAR OPERATIONS COMMISSION 2025

through the sending of a PAN. He must be informed of the facts and the law upon which the assessment is made. The law imposes a substantive, not merely a formal, requirement. To proceed heedlessly with tax collection without first establishing a valid assessment is evidently violative of the cardinal principle in administrative investigations — that taxpayers should be able to present their case and adduce supporting evidence. (*CIR vs. Avon Products Manufacturing, G.R. Nos. 201398-99, October 03, 2018*)

The right to due process is violated when the taxpayer receives both the PAN and the FAN on the same day. The failure to give the taxpayer the opportunity to respond to the PAN makes the assessment void. (*CIR vs. Yumex Philippines Corporation, CTA EB Case No. 1139, 11 August 2015*)

BIR violated taxpayer's right to due process by issuing a FAN without even awaiting its reply to the PAN. (*Prime Steel Mill, Incorporated vs CIR, G.R. No. 249153, September 12, 2022*)

Default in PAN

If the taxpayer fails to respond within fifteen (15) days from date of receipt of the PAN, he shall be considered in default, in which case, a formal letter of demand and assessment notice shall be caused to be issued by the said Office, calling for the payment of the taxpayer's deficiency tax liability, inclusive of the applicable penalties.

Absence of PAN

The issuance of the PAN is part of the due process requirement. Thus, if the BIR did not issue a PAN or did not give the taxpayer an opportunity to respond within 15 days, this will be a violation of the due process right of a taxpayer. (*Metro Star Superama, Inc. vs. CIR, G.R. No. 185371, December 8, 2010*)

v. Issuance of Formal Letter of Demand (FLD) / Final Assessment Notice (FAN)

Definition of FLD/FAN

An FLD/FAN is a written demand to pay deficiency taxes fated to a taxpayer who fails to respond to a PAN within the prescriptive period of time, or whose reply to the PAN was found to be without merit, whether in full or in part.

An assessment contains not only a computation of tax liabilities, but also a demand for payment with a prescribed period.

FLD/FAN calling for payment of taxes must include the facts, law, rules and regulations, and jurisprudence upon which it is based. Otherwise, it shall be void. (*Section 228, NIRC; RR No. 18-2013, RMC No. 11-2014*)

15-day Period Rule

The taxpayer has fifteen (15) days from the date of receipt of the PAN to respond to the said notice. Only after receiving the taxpayer's response or in case of the taxpayer's default can the BIR issue the FLD/FAN. (*Prime Steel Mill, Inc. vs. CIR, G.R. No. 249153, September 12, 2022*)

The failure to file a reply to PAN will not bar the taxpayer from protesting the FAN. (*RMO No. 26-2016*)

Protest against the PAN is optional and **NOT MANDATORY**. (*RR No. 18-2013*)

Requisites of a Valid FAN/FLD

1. A FAN/FLD must be in writing and signed by the BIR;
2. A FAN/FLD must contain the law and the facts on which the assessment is based (ie., the basis must be provided);
3. Contains a demand for payment within the prescribed period;
4. The FAN/FLD must be served on and received by the taxpayer,

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Best Evidence Rule

The Commissioner of Internal Revenue may use the best evidence obtainable to issue an assessment under the following circumstances:

1. When a report required by law as a basis for the assessment of any national internal revenue tax shall not be forthcoming within the time fixed by laws or rules and regulations; or
2. When there is reason to believe that any such report is false, incomplete, or erroneous. *(Section 6, NIRC, as amended)*

Purpose of Due Process Requirement

Taxpayers should be informed of the facts and the law on which the assessments are based conforms with the constitutional mandate that no person shall be deprived of his or her property without due process of law.

Between the power of the State to tax and an individual's right to due process, the scale favors the right of the taxpayer to due process.

The purpose of the written notice requirement is to aid the taxpayer in making a reasonable protest, if necessary. Merely notifying the taxpayer of his or her tax liabilities without details or particulars is not enough. *(CIR vs Fitness by Design Inc., G.R. No. 215957, November 09, 2016)*

Distinguish PAN from FAN

PAN	FAN
A PAN merely informs the taxpayer of the initial findings of the Bureau of Internal Revenue. It contains the proposed assessment, and the facts, law, rules, and regulations or jurisprudence on which the proposed assessment is based. It does not contain a demand for payment but usually requires the	On the other hand, a FAN contains not only a computation of tax liabilities but also a demand for payment within a prescribed period. As soon as it is served, an obligation arises on the part of the taxpayer concerned to pay the amount assessed and

PAN	FAN
taxpayer to reply within 15 days from receipt. Otherwise, the CIR will finalize an assessment and issue a FAN. The PAN is a part of due process. It gives both the taxpayer and the CIR the opportunity to settle the case at the earliest possible time without the need for the issuance of a FAN.	demand. It also signals the time when penalties and interests begin to accrue against the taxpayer.
Contents	
Contains PROPOSED assessments	Computation of tax liabilities
Does not contain a demand for payment	Contains demand for payment within a prescribed period

(CIR vs. Transition Optical Philippines, G.R. No. 227544, November 22, 2017).

Related Jurisprudence

The Supreme Court held that although the CIR presented the registry receipt and certification of the Postmaster and it had testimonies of those who personally delivered the mail matter to the post, the administrative officer of SM City Pampanga who allegedly received the FLD-FAN, was not presented to testify on her functions and to confirm that she indeed received such mail matter. There is also no showing that a Preliminary Collection Letter was issued by the BIR and received by the taxpayer.

Significantly, the CIR failed to prove compliance with the two requisites under Sec. 3.1.7 of RR No. 12-99 on effecting constructive service: (1) leaving the notice in the premises of the taxpayer, and (2) the fact of such service is attested to, witnessed, and signed by at least two revenue officers other than the revenue officer who constructively served the same. Without proof that these two requisites had been duly complied with, service of the FLD-DDAN at the ground floor of the administrative

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office of SM City Pampanga cannot be deemed constructive service to the taxpayer.

Thus, the CIR's failure to prove that the FLD-FAN was properly served on taxpayer by registered mail renders void the deficiency assessment issued by the CIR (*CIR vs. South Entertainment Gallery, Inc.*, G.R. No. 2237667, April 24, 2023)

The SC held that the CIR failed to properly serve the assessment notices upon taxpayer. It is undisputed that the NIC, the PAN, and the FAN bear indications that they were personally served. However, those who received them were not authorized representatives of the taxpayer. (*Mannasoft Technology Corporation vs. CIR*, G.R. No. 244202, July 10, 2023)

There can be no substantial compliance with the due process requirement when the BIR completely ignored the 15-day period by issuing the FAN and FLD even before the petitioner was able to submit its Reply to the PAN. (*Prime Steel Mill, Incorporated v. CIR*, G.R. No. 249153, September 12, 2022)

The SC held that FAN issued by the CIR does not comply with the requirements under Section 228, NIRC, as amended because the notice failed to state the factual and legal bases upon which the assessment was made. (*CIR vs. Unioil Corporation*, G.R. No. 204405, August 04, 2021)

Consequently, the FAN was void and Unioil was deprived of due process. Further, the FAN, being invalid, did not effectively toll the three (3)-year period for the BIR to assess deficiency taxes. (*Id.*)

The Supreme Court held that Yumex was not given any notice of the preliminary assessment at all and was deprived of the opportunity to respond to the same before being given the final assessment. That Yumex was able to file a protest to the FLD/FAN is of no moment. Neither does the payment by Yumex of the other items in the FLD/FAN, preclude it from questioning the validity of the issuance of the

assessment notices. The fact that the taxpayer's right to due process was violated because it was denied the opportunity to respond to the PAN remains glaringly evident and cannot be deemed erased or cured by the taxpayer's volitional payment of other assessed items. (*CIR vs. Yumex Philippines, Corporation*, G.R. No. 222476, May 05, 2021)

The SC held that the CIR was not able to sufficiently prove that the PAN and the FAN were properly and duly served upon and received by the taxpayer. In view of the taxpayer's categorical denial of due receipt of the PAN and the FAN, the burden was shifted to the CIR to prove that the mailed assessment notices were indeed received by it or by its authorized representatives.

The CIR's mere presentation of Registry Receipts was insufficient to prove receipt of the PAN and the FAN. The witnesses for the CIR failed to identify and authenticate the signatures appearing on the registry receipts; thus, it cannot be ascertained whether the signatures appearing in the documents were those of taxpayer's authorized representatives. (*CIR vs. T. Shuttle Services, Inc.*, G.R. No. 240729, August 24, 2020)

FAN/FLD issued by the BIR even before the lapse of 15-day period within which the taxpayer could file a reply or protest to PAN is void. (*Missouri Square v. CIR*, CTA Case No. 87070, September 8, 2016)

Non-service of PAN amounts to denial of due process. Thus, the FAN/FLD were deemed void. (*Bloat & Ogle v. CIR*, CTA Case No 8682, September 2, 2016)

BIR was found to violate the due process requirement when it served both the PAN and FAN/FLD on the same day. (*CIR v. Yumex*, CTA EB No. 1139, September 7, 2011)

A FAN/FLD was considered void for not having an assessment notice attached even though the FLD stated the following:

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- a. Computation or tabulation of the alleged deficiency tax, together with interest and penalties and their respective basis.
- b. A request to pay deficiency taxes thru an authorized agent bank
- c. A note that the interest will be adjusted if the total amount is paid beyond a certain date.

The above statements did not amount to an "assessment notice" – as there was no mention of a definite time when payment was due and demandable. (*Derek Ramsay v. CIR, CTA Case 8456, September 17, 2015*)

a. Prescriptive Period of Assessment

Concept of Prescription

The right of the BIR to assess and collect taxes from taxpayers is not unlimited. Prescription can be treated as the time limit imposed by law for the BIR to initiate assessment and collection proceedings.

Accordingly, assessments issued after the expiration of such period are no longer valid and effective. (*CIR vs. System Technology Institute, Inc., G.R. No. 220835, June 26, 2017*)

Reason for Prescription

a. To the government: Officers would be obliged to act properly and promptly in making assessments.

b. To the taxpayers:

- To provide a feeling of security against unjust tax audit.
- To provide a limit on obligation to keep their books and for inspection.

The very reason why the law provided for prescription is to give taxpayers peace of mind, that is, to safeguard them from unreasonable examination, investigation, or assessment. (*CIR vs*

Standard Chartered Bank, G.R. NO. 192173, July 29, 2015)

When Assessment is Made

An assessment is deemed made only when the CIR releases, mails or sends such notice to the taxpayer. (*CIR vs. B.F. Goodrich Phils., Inc., G.R. No. 104171, February 24, 1999*)

The assessment contemplated in Sections 203 and 222 refers to the service of the FAN upon the taxpayer. (*CIR vs Pascor Realty and Development Corporation, et. al., G.R. No. 128315, June 29, 1999*)

Accordingly, it is the issuance of FAN/FLD that must fall within the prescriptive periods for assessment. Further, the prescriptive period for collection is reckoned from the issuance of the FAN/FLD.

The assessment is deemed made when notice to this effect is released, mailed, or sent by the BIR to the taxpayer within the prescriptive period. It is not required that the assessment notice be received by the taxpayer before the lapse of the prescriptive period for assessment. (*Basilan Estates, Inc. vs. CIR, G.R. No. L-22492, September 5, 1967*)

Prescriptive Period

Ordinary Prescription

General Rule: Taxes shall be assessed within three (3) years after either:

- a. The last day prescribed by law for the filing of the return;
- b. The actual filing of the return, whichever is later (*Section 203, NIRC, as amended*)

Effect of Amendment of Returns on reckoning of the Prescriptive period

Taxpayers have the right to amend taxes as many times so long as it is done within (3) years from the date it was filed, *provided no notice for audit or investigation was received from the BIR.*

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However, an amendment of a return may or may not affect the running of the prescriptive period: If such amendment is considered a "*substantial amendment*" – one that would decrease or increase the tax payable. The three-year prescriptive period will start to run from the date when the amended return was filed. (*CIR vs. Phoenix Assurance Co., Ltd., G.R. No. L-19727, May 20, 1965*)

Extra-ordinary prescription

Exception to Ordinary Prescription:

a. The tax may be assessed, or a proceeding in court for the collection of such tax may be filed without assessment, at any time **within ten (10) years after the discovery** of either of the following:

1. False return, (regardless of intent to evade tax);
2. Fraudulent return with intent to evade tax; or
3. Failure to file a return, as in the case of a wrong return or a grossly defective

b. If before the expiration of the three-year prescriptive period for the assessment of the tax, both the Commissioner and the taxpayer have agreed in writing to its assessment after such time. The period so agreed upon may be extended by a subsequent written agreement made before the expiration of the period previously agreed upon (*Section 222, NIRC, as amended*).

Summary of Prescriptive Period for Assessment and Collection

Description	Prescriptive period of Assessment	*Prescriptive period of Collection
Ordinary Prescription		
Return was filed before due date	3 years from due date (<i>Sec. 203, NIRC</i>)	May be collected by distraint, levy or court actions within 3 years from the date the FLD/FAN was released, mailed or sent by the BIR
Return was filed on due date	3 years from due date (<i>Sec. 203, NIRC</i>)	
Return was filed after due date	3 years from filing date (<i>Sec. 203, NIRC</i>)	

Description	Prescriptive period of Assessment	*Prescriptive period of Collection
Return was substantially amended	3 years from filing of substantial amendment (<i>CIR v. Phoenix Assurance, G.R. No. L-19727, May 20, 1965</i>)	to the TP. (<i>Sec. 203, NIRC</i>)
Extraordinary Prescription		
False return, Fraudulent return with intent to evade tax, failure to file return	10 years from the " discovery " of the falsity, fraud, or failure to file return.	May be collected by distraint, levy or court actions within 5 years following the assessment. (<i>Sec. 222, NIRC; La Flor dela Isabela v. CIR, GR 202105, April 28, 2021</i>)

**Note: This was clarified by the Supreme Court in Commissioner of Internal Revenue vs. Court of Tax Appeals Second Division, G.R. No. 258947, March 29, 2022 citing the case of CIR v. United Salvage and Towage (Phils.), Inc. G.R. No. 197515, July 2, 2014.*

1. False Returns vs Fraudulent Return vs Non-filing of Returns

False Returns	Fraudulent Returns	Non-Filing of Returns
There is a deviation from the truth, whether intentional or not. It may be due to mistake, ignorance, or carelessness	Implies intentional or deceitful entry with intent to evade the taxes due	Failure or Omission to file a return
Does not make the taxpayer criminally liable	Filing a Fraudulent return will make you liable for crimes involving moral turpitude as it entails willfulness and fraudulent intent on the	Mere omission is already a violation regardless of the fraudulent intent or willfulness of the individual (<i>CIR v.</i>

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False Returns	Fraudulent Returns	Non-Filing of Returns
	part of the individual (Republic v. Marcos II, G.R. No. 130855, August 4, 2009)	Bank of Commerce, CTA EB No. 654, March 14, 2011)

Filing of a FALSE Return

When there is a showing that a taxpayer has substantially under-declared its sales, receipt or income, there is a presumption that it has filed a false return. As such, the CIR need not immediately present evidence to support the falsity of the return, unless the taxpayer fails to overcome the presumption against it. (*Far Eastern University vs. City of Manila*, CTA AC No. 223, October 14, 2020, citing *CIR vs. Asalus Corporation*, G.R. No. 221590, February 22, 2017)

While the filing of a fraudulent return necessarily implies that the act of the taxpayer was intentional and done with intent to evade the taxes due, the filing of a false return can be intentional or due to honest mistake. (*CIR vs. Philippine Daily Inquirer*, G.R. No. 213943, March 22, 2017)

A false return simply involves a "deviation from the truth, whether intentional or not" while a fraudulent return "implies intentional or deceitful entry with intent to evade the taxes due." (*CIR vs. United Church of Christ*, CTA EB Case No. 2346, March 15, 2022, citing *Commissioner vs. Fitness by Design*, G.R. No. 215957, November 09, 2016)

The settled rule is that "the entry of wrong information due to mistake, carelessness, or ignorance, without intent to evade tax, does not constitute a false return." That, there is an under/overstatement, by itself, does not amount to a falsehood for purposes of

extending the assessment period. (*McDonald's Philippines Realty Corp. vs. CIR Revenue*, G.R. No. 247737, August 8, 2023, citing *CIR vs. B.F. Goodrich Phils., Inc.*, G.R. No. 104171, February 24, 1999; *CIR vs. Philippine Daily Inquirer, Inc.*, G.R. No. 213943, March 22, 2017; *CIR vs. Spouses Magaan*, G.R. No. 232663, May 3, 2021; *CIR vs. Unioil Corporation (Unioil)*, G.R. No. 204405, August 4, 2021.

Filing of a FRAUDULENT Return

Fraud is a question of fact that should be alleged and duly proven. "The willful neglect to file the required tax return or the fraudulent intent to evade the payment of taxes, considering that the same is accompanied by legal consequences, cannot be presumed." Fraud entails corresponding sanctions under the tax law. Therefore, it is indispensable for the CIR to include the basis for its allegations of fraud in the assess notice. Here, the (the BIR investigating officer) admitted that the gathered information did not show that the respondent deliberately failed to reflect its true income in 1995. (*CIR vs. Miffi Logistics Co., Inc.*, CTA EB Case No. 1979, January 23, 2020, citing *Commissioner vs. Fitness by Design*, G.R. No. 215957, November 09, 2016)

For the ten-year period under Section 222(a) to apply, it is not enough that fraud is alleged in the complaint, it must be established by clear and convincing evidence. The petitioner, having failed to discharge the burden of proving fraud, cannot invoke Section 222(a). (*Republic v. GMCC United Development Corp.*, G.R. No. 191856, December 7, 2016)

Fraud must be alleged and proved as a fact. It must be the product of a deliberate intent to evade taxes. It may be established by the integration of three factors:

- a. Intentional and substantial understatement of tax liability by the taxpayer;
- b. Intentional and substantial overstatement of deductions or exemptions; and/or

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c. Recurrence of the above circumstances. (*CIR vs. Estate of Benigno Toda Jr*, G.R. No. 147188, September 14, 2004)

purpose of tax evasion. (*CIR vs. Unioil Corporation*, G.R. No. 204405, August 04, 2021)

Fraud-related decisions:

a. Fraud must be the product of a deliberate intent to evade taxes; (*Commissioner vs. Fitness by Design*, G.R. No. 215957, November 09, 2016)

b. Simple statement that the return filed was not fraudulent does not disprove existence of fraud; and

c. Presence of fictitious expenses, with no evidence presented, proves existence of fraud.

However, the courts did not consider the tax returns filed as false or fraudulent with intent to evade payment of tax in the following cases:

- a. Mere understatement in the tax return will not necessarily imply fraud;
- b. Sale of a real property for a price less than its fair market value is not necessarily a false return;
- c. Fraud is a question of fact and the circumstances constituting fraud must be alleged and proved in the trial court;
- d. Fraud is never imputed and the courts never sustain findings of fraud upon circumstances that only create suspicion; and
- e. Mistakes of revenue officers on three different occasions remove elements of fraud.

In determining whether the return filed is false or fraudulent, jurisprudence has consistently held that fraud is never imputed. The Court has refrained from sustaining findings of fraud upon circumstances which, at most, create only suspicion. The mere understatement of a tax is not itself proof of fraud for the

Prima facie evidence of Fraudulent Return.

There is prima facie evidence of fraud if the taxpayer:

a. substantially underdeclared their taxable sales, receipts or income, or

b. substantially overstated their deductions.

Failure to report sales, receipts or income in an amount exceeding 30% of that declared per return, and a claim of deduction in an amount exceeding 30% of actual deduction shall render the taxpayer liable for substantial underdeclaration and overdeclaration. (*Section 248, NIRC, as amended*)

If the CIR is able to establish a prima facie evidence of fraud, the burden of proof shifts to the taxpayer to prove that there is no fraud committed.

Application of the 10-Year Prescriptive Period

Requirements to Apply the 10-Year Prescriptive Period The following are the requirements to warrant the application of the extraordinary prescriptive period of 10 years:

a. Proof of False, Fraudulent or Failure to File a Return - The extraordinary 10-year assessment period may apply in case the taxpayer: (1) filed a false return, (2) filed a fraudulent return, or (3) failed to file a return.

A fraudulent return "implies intentional or deceitful entry with intent to evade the taxes due," while a false return simply "implies deviation from the truth, whether intentional or not."

It must be stressed, however, that a false return within the meaning of Section 222(a) does not refer to false returns in general. To be

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sure, the extraordinary 10-year assessment period applies to a false return when:

- i. the return contains an error or misstatement, and
- ii. such error or misstatement was deliberate or willful.

It shall be the CIR's burden to establish the existence of the above-enumerated statutory requisites with clear and convincing evidence.

Exception to the proof required:

Prima facie evidence of fraud - The CIR may be relieved from the above-mentioned burden of proof when there is prima facie evidence of falsity or fraud as discussed above.

If the 30% threshold satisfied, there is prima facie evidence of falsity or fraud and the burden of proof shifts to the taxpayer.

- i. If the taxpayer fails to overcome the presumption, the prima facie evidence shall be sufficient to justify the application of the 10-year period.
- ii. If the taxpayer is successful in overturning the presumption (e.g., demonstrating that the misstatement as ascertained by the CIR had been inadvertent or attributable to a mistake or was not deliberate or willful on the part of the taxpayer), the CIR cannot rely on the presumption in proving the taxpayer's intent to evade. (*McDonald's Philippines, Realty Corp. vs CIR, G.R. No. 247737, August 8, 2023*)

Due Process Requirements before the extraordinary 10- year prescriptive period for assessment may be applied

I. First Due Process Requirement

The assessment notice issued to the taxpayer must clearly state the following:

- a. that extraordinary prescriptive period (not the basic three-year period) is being applied, and

b. the bases of allegations of falsity or fraud (e.g., if the CIR seeks to rely on the presumption of falsity or fraud particularly, the formal notice to the taxpayer must set out the computation by which it ascertained that the misdeclaration in the return surpassed the 30% threshold).

II. Second Due Process Requirement.

The tax authorities have not acted in a manner that is inconsistent with the invocation of the extraordinary prescriptive period or have otherwise misled the taxpayer that the basic period will be applied.

The law on prescription, being a remedial measure, should be liberally construed in order to afford such protection.

As a corollary, the exceptions to the law on prescription should perforce be strictly construed. (*McDonald's Philippines, Realty Corp. vs CIR, G.R. No. 247737, August 8, 2023; CIR vs. B.F. Goodrich Phils., Inc., G.R. No. 104171, February 24, 1999*)

Defective Return

A wrong return, however, is different from a defective return. Defective returns may be sufficient if there is substantial compliance.

There is substantial compliance when:

- a. The return is made in good faith and is not false or fraudulent;
- b. It covers the entire period involved; and
- c. It contains information as to the various items of income, deduction and credit with such definiteness as to permit the computation and assessment of the tax (*CIR vs. Lilia Gonzales, G.R. No. L-19495, April 2, 1919*).

Non-Filing of Return

A deficient return which prevented the CIR from computing taxes due; such return is the same as if no return is filed at all (*CIR v. Gonzales, G.R. No. L-19495, 1966*)

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Failure to report income in the returns which were clearly not exempted from tax – CTA did not treat it as a simple omission since it involved substantial sums (*Standard Chartered Bank vs. CIR, CTA EB Case No. 731, September 13, 2012*)

Nothing in Sec. 222(A) shall be construed to authorize the examination and investigation or inquiry into any tax return filed in accordance with the provisions of any tax amnesty law or decree.

Amended Return

The nature of the amendment of its return is determinative of the prescriptibility of the assessment. (*Lapanday Foods Corporation vs. CIR, G.R. No. 186155, January 17, 2023*)

Accordingly, if the taxpayer files an amended return which is substantially different from the original return, prescription is counted from the filing of the amended return.

Amendment is considered substantial if:

- a. There is underdeclaration (exceeding 30%) of taxable sales, receipts or income; or
- b. There is overstatement (exceeding 30%) of deductions. (*Section 248(B), NIRC, as amended*)

Waiver of the Statute of Limitations

The CIR or their duly authorized representative and the taxpayer or their authorized representative may agree in writing as to a specific future date within which to assess the taxpayer for internal revenue taxes for a given taxable period, before the expiration of the period to assess taxes. (*Section 222(B), NIRC, as amended*)

The waiver is not a waiver of the right to invoke the defense of prescription. Rather, it is an agreement between the taxpayer and the BIR to extend the period to a date certain, within which the latter could still assess or collect taxes due. (*Bank of the Philippines, Inc. vs. CIR, G.R. No. 139736, October 17, 2005*)

While the waiver extends the prescriptive period, it has been held that the CIR cannot validly agree to reduce the prescriptive period to less than that granted by law because it would result to the detriment of the State. (*Republic vs. Lopez, G.R. No. L-18007, March 30, 1967*)

The taxpayer's waiver of statute of limitation does not cover taxes already prescribed. (*Republic vs. Lim De Yu, G.R. No. L-17438, April 30, 1964*.)

Accordingly, the Waiver of the Statute of Limitations shall be executed before the expiration of the period to assess or to collect taxes (*Id.*)

Guidelines on Proper Execution of Waiver

For a Waiver of the defense of prescription to be valid, the following guidelines should be taken into account:

1. The Waiver is a unilateral and voluntary undertaking that takes legal effect on the taxpayer immediately upon execution.
2. The Waiver need not specify the taxes to be assessed nor the amount thereof.
3. The delegation of authority to a representative need not be in writing and notarized
4. The taxpayer cannot invalidate the Waiver by contesting the authority of his own representative.
5. The taxpayer shall submit his Waiver to the officials prior to the expiration of the period to assess or to collect.
6. The Revenue District Officer or Group Supervisor designated in the Letter of Authority or Memorandum of Assignment can accept the Waiver.
7. The date of acceptance by the BIR Officer is no longer required to be indicated.

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8. The taxpayer shall retain a copy of the submitted Waiver.

9. Notarization of the Waiver is not a requirement for its validity.

10. The taxpayer must ensure that his Waiver:

- is executed before the expiration of the period to assess or to collect taxes;
- indicates the expiry date of the extended period;
- it indicates the type of tax (for waiver of the prescriptive period to collect); and
- is signed by his authorized representative.

11. There is no strict format for the Waiver. The taxpayer may utilize any form with no effect on its validity (*RMC No. 141-2019*)

Estoppel on Prescription

The doctrine of estoppel may prevent the taxpayer from raising the defense of prescription against the efforts of the government to collect the assessed tax. In one case, there was a finding that the taxpayer made several requests or positive acts to convince the government to postpone the collection of taxes. (*Collector of Internal Revenue vs. Suyoc Consolidating Mining, Co., G.R. No. L-11527, November 25, 1958*)

If the defects noted in the waivers were not solely attributable to the CIR, estoppel may also apply. A careful reading of RDAO 01-05 indicates that the proper preparation of the waiver was primarily the responsibility of the taxpayer or its authorized representative signing the waiver. Such responsibility did not pertain to the BIR as the receiving party. The SC held that the taxpayer was not correct in insisting that the act or omission giving rise to the defects of the waivers should be ascribed solely to the CIR and her subordinates (*Asian Transmission Corporation vs. CIR, G.R. No. 230861, September 19, 2018*)

Execution of the waivers was to the advantage of the taxpayer because the waivers would

provide the taxpayer the sufficient time to gather and produce voluminous records for the audit. It would really be unfair, therefore, were the taxpayer to be permitted to assail the waivers only after the final assessment proved to be adverse. (*Id.*)

The parties are in *pari delicto* or "in equal fault." In *pari delicto* connotes that the two parties to a controversy are equally culpable or guilty and they shall have no action against each other. The Supreme Court said that to uphold the validity of the Waivers would be consistent with the public policy embodied in the principle that taxes are the lifeblood of the government, and their prompt and certain availability is an imperious need. As between the parties, it would be more equitable if the CIR's lapses were allowed to pass and consequently uphold the Waivers in order to support this principle and public policy. The Court pronounced that parties must come to court with clean hands. Parties who do not come to court with clean hands cannot be allowed to benefit from their own wrongdoing. Following the foregoing principle, the taxpayer should not be allowed to benefit from the flaws in its own Waivers and successfully insist on their invalidity in order to evade its responsibility to pay taxes. (*CIR vs. Next Mobile, Inc. G.R. No. 212825, December 7, 2015*)

The SC ruled that the taxpayer after voluntarily executing waivers, insisted on their invalidity by raising the very same defects it caused. On the other hand, the BIR miserably failed to exact from the taxpayer compliance with its rules. The BIR's negligence in the performance of its duties was so gross that it amounted to malice and bad faith. Moreover, the BIR was so lax such that it seemed that it consented to the mistakes in the Waivers. Such a situation is dangerous and open to abuse by unscrupulous taxpayers who intend to escape their responsibility to pay taxes by mere expedient of hiding behind technicalities. (*Id.*)

If the taxpayer never raised the invalidity of the Waivers at the earliest opportunity, either in its

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Protest to the PAN or Protest to the FAN, that is an implied recognition of the Waivers' validity and its representatives' authority to execute them. The Court observed in one case that the taxpayer only raised the issue of these Waivers' validity in its Petition for Review filed with the Court of Tax Appeals. (*CIR vs. Transnational Optical Philippines, Inc., G.R. No. 227544, November 22, 2017*)

b. Suspension of Statutes of Limitation for Assessment and/or Collection

The following suspends the running of the prescriptive period:

1. The taxpayer cannot be located in the address given by them in the return.

Exception: The CIR is informed of change in address.

2. The taxpayer is out of the Philippines.

3. The taxpayer requests for reinvestigation which is granted by the CIR.

4. The warrant, distraint and levy is duly served and no property is located.

This only suspends the prescriptive period for collection.

5. Where the CIR is prohibited from assessing or beginning distraint or levy or a proceeding in court for 60 days thereafter, such as where there is a pending petition for review in the CTA from the decision on the protested assessment, such suspends the running of the prescriptive period for collection (*Republic vs. Ker & Co., G.R. No. L-21609, September 29, 1966*)

6. When there is an Answer filed by the BIR to the petition for review in the CTA, where the court justified this by saying that in the answer filed by the BIR, it prayed for the collection of taxes. (*Hermanos vs. CIR, G.R. No. L-24972, September 30, 1969*)

A motion for reconsideration does not suspend the running of three-year prescriptive period.

(*ESS Manufacturing Co., Inc. vs. CIR, G.R. Nos. 226177, 226212 & 226232 (Notice), August 22, 2022.*)

d. Collection Process

i. Requisites

The requisites for the exercise of the government of its remedies for the collection of delinquent taxes:

1. The taxpayer's protest against the FLD/FAN has been denied by the BIR, or the assessment has become final and executory.

2. Collection must be made before the lapse of the prescriptive period for collection. (*Section 222(b), NIRC, as amended*)

Civil Action for the collection of internal revenue taxes instituted:

A civil action may be resorted to when a tax liability becomes collectible which means that an assessment was made and such assessment becomes final and unappealable or the decision of the CIR has become final, executory, and demandable.

This occurs when:

a. A tax is assessed and the taxpayer fails to file an administrative protest by filing a request for reconsideration or reinvestigation within thirty (30) days from receipt of the assessment.

b. A protest against the assessment is filed by the taxpayer but the CIR's decision denying in whole or in part the said protest was not appealed to the CTA within thirty (30) days from receipt of such decision. (*Section 228, NIRC, as amended*)

Judicial Action for the collection of internal revenue taxes instituted:

A judicial action for the collection of a tax is instituted:

a. by the filing of a complaint with the court of competent jurisdiction; or

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b. where the assessment is appealed to the Court of Tax Appeals, by filing an answer to the taxpayer's petition for review wherein payment of the tax is prayed for. (*CIR vs. Pilipinas Shell Petroleum Corporation, G.R. Nos. 197945 & 204119, July 09, 2018*)

Court Action for Collection of Taxes

As a general rule, no proceeding in court without assessment for the collection of such taxes shall be begun after the expiration of 3-year prescriptive period for the assessment. (*Section 203, NIRC, as amended*)

The exception is in case of filing of a False or Fraudulent Return or Failure to File a return, in which case, a direct court action for collection of taxes may be initiated. (*Section 222, NIRC, as amended*)

ii. Prescriptive Periods

In cases of assessments issued within the three-year ordinary period, the CIR has another three years within which to collect taxes. For assessments issued within the extraordinary period of 10 years in cases of false or fraudulent return or failure to file a return, the period for collection of taxes shall be five (5) years. (*CIR vs. CTA, G.R. No. 258947, March 29, 2022*)

Exceptions:

a. In the case of a false or fraudulent return with intent to evade tax or of failure to file a return, the tax may be assessed, at any time within ten (10) years after the discovery of the falsity, fraud, or omission. Any internal revenue tax that has been assessed in this manner may be collected by distraint or levy or by a proceeding in court within five (5) years following the assessment of the tax.

b. In the case of a false or fraudulent return with intent to evade tax or of failure to file a return, a proceeding in court for the collection of such tax may be filed without assessment, at any time within ten (10) years after the discovery of the falsity, fraud or omission;

c. If before the expiration of the time prescribed for the assessment of the tax, both the Commissioner and the taxpayer have agreed in writing to its assessment after such time, the tax may be assessed within the period agreed upon. The period so agreed upon may be extended by subsequent written agreement made before the expiration of the period previously agreed upon. Any internal revenue tax which has been assessed in this manner may be collected by distraint or levy or by a proceeding in court within five (5) years following the assessment of the tax. (*Section 222, NIRC, as amended*)

e. Taxpayers Remedies

i. Protesting an Assessment

Requisites of a Valid Protest:

1. In writing;
2. Addressed to the CIR;
3. Accompanied by a waiver of the Statute of Limitations in favor of the Government. Without the waiver, the prescriptive period will not be tolled;
4. State the facts, applicable law, rules and regulations or jurisprudence on which the protest is based otherwise the protest would be void; and
5. Must contain the following:
 - a. Name of the taxpayer and address for the immediate past 3 taxable years;
 - b. Nature of the request, specifying the newly discovered evidence to be presented;
 - c. Taxable periods covered by the assessment;
 - d. Amount and kind of tax involved and the assessment notice number;
 - e. Date of receipt of the assessment notice or letter of demand;
 - f. Itemized statement of the finding to which the taxpayer agrees (if any) as basis for the computation of the tax due,

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ARELLANO UNIVERSITY SCHOOL OF LAW BAR OPERATIONS COMMISSION 2025

which must be paid upon filing of the protest;

- g. Itemized schedule of the adjustments to which the taxpayer does not agree;
- h. Statements of facts or law in support of the protest; and
- i. Documentary evidence as it may deem necessary and relevant to support its protest to be submitted 60 days from the filing thereof.

NOTE: RR 18-13 mandates that **protests should include the facts, law, rules, regulations on which the protest is based. Otherwise, the protest is void and of no effect.**

If there are *several issues* involved in the FLD/FAN but the taxpayer only disputes or protests against the validity of some of them, the items not properly protested shall become final and demandable and a collection letter shall be issued immediately.

Distinguish Request for Reconsideration from Request for Reinvestigation

Request for Reconsideration	Request for Reinvestigation
Refers to a plea of reevaluation of an assessment on the basis of existing records WITHOUT need of additional evidence.	Refers to a plea of reevaluation of an assessment on the basis of newly discovered or ADDITIONAL EVIDENCE that a taxpayer intends to present in the reinvestigation.
No need to submit additional evidence	Taxpayer is given 60 days from the filing the request for reinvestigation to provide all relevant supporting documents , otherwise the

Request for Reconsideration	Request for Reinvestigation
	assessment is final, executory, due and demandable.
It does not toll the running of the prescriptive period for the collection of an assessed tax	It tolls the prescriptive period to collect if the request for reinvestigation is granted by the BIR
Reckoning day of 180 days inaction by CIR or its duly authorized representative is based from the date of filing of request for reconsideration	Reckoning day of 180 days inaction by CIR or its duly authorized representative is based from the date of filing of the relevant supporting documents

a. Period to file the Protest

The taxpayer or its authorized representative or tax agent may protest administratively against the aforesaid FLD/FAN **within thirty (30) days from date of receipt** thereof.

2. Effect of Failure to File Protest

When no protest is seasonably made by the taxpayer, the assessment shall become final, executory and demandable, and no request for reconsideration or reinvestigation shall be granted thereon. (*RR No. 12 - 99, as amended by RR No. 18 - 13*)

ii. Submission of Supporting Documents by Taxpayer

Within sixty (60) days from filing of the protest, all relevant supporting documents must be submitted, otherwise the assessment shall become final. (*Section 228 of the NIRC*)

The BIR requires an identification of the kind of protest filed – whether a reconsideration or reinvestigation. The submission of additional documents within 60 days from filing of protest

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ARELLANO UNIVERSITY SCHOOL OF LAW BAR OPERATIONS COMMISSION 2025

is allowed only in the case of reinvestigation. For motion for reconsideration, the decision of the BIR will be based only on documents already submitted to the BIR prior to the issuance of FAN and no new evidence will be accepted. (*RR No. 18-2013*)

The taxpayer can still submit the pertinent supporting documents and additional explanations within sixty (60) days from the date of filing the request for reinvestigation. However, the BIR issued the Final Decision on Disputed Assessment (FDDA) after the lapse of only thirty (30) days. The Supreme Court declared the assessment against the taxpayer null and void on the ground of the manifest violation of the taxpayer's right to due process. The Court took the opportunity to definitely settle that the reckoning point of the sixty (60) day period for the submission of relevant supporting documents is from the filing of the administrative protest to the FLD/FAN when such protest constitutes a request for reinvestigation, and not from the response or reply to the PAN. (*CIR vs. Maxicare Healthcare Corporation, G.R. No. 261065*)

Relevant Supporting Documents

The CIR cannot demand other supporting documents, particularly if they do not exist and eventually hold that failure to provide within the 60-day period makes the assessment final and executory. "The term **"relevant supporting documents"** should be understood as those documents necessary to support the legal basis in disputing a tax assessment as determined by the taxpayer. The BIR can only inform the taxpayer to submit additional documents. The BIR cannot demand what type of supporting documents should be submitted. Otherwise, a taxpayer will be at the mercy of the BIR, which may require the production of documents that a taxpayer cannot submit." (*CIR vs. First Express Pawnshop Company, Inc., GR No. 172045-46, June 16, 2009*)

iii. Decision of the Commissioner on the Protest

a. Period to Act Upon or Decide on Protest Filed

The CIR has 180 days from the date of:

1. Filing of the protest, in case of a request for reconsideration; or
2. Submission by the taxpayer of the required documents within 60 days from filing of the protest, in case of a request for reinvestigation.

Decision on the Protest Filed by the CIR or its duly authorized representative.

(1) Approval of the Protest – Based on the justification provided by the taxpayer, the BIR grants the protest and dismisses its claim against the taxpayer terminating the audit case against him/her.

(2) Denial of the Protest – this could either be:

a. Direct Denial of Protest

The protest may be denied through the issuance of Final Decision of Disputed Assessment, stating the facts, applicable law, rules and regulations or jurisprudence on which such decision is based otherwise, the decision shall be void in which case the same shall not be considered a decision on a disputed assessment and that the same is his final decision. (*RR No. 12-99*)

b. Indirect Denial of Protest

An indirect denial of protest results if the CIR through its actions, in relation to a pending protest, does either of the following:

1. **Inaction** by the CIR within the 180-day period (*Sec. 228, last par., NIRC*) provided to act upon a protest.
2. Filing of a **collection case** before the regular courts for the collection of the tax. (*Yabes vs. Flojo, G.R. No. L-46954, July 20, 1982*)

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ARELLANO UNIVERSITY SCHOOL OF LAW BAR OPERATIONS COMMISSION 2025

3. Issuance of a **warrant of distraint or levy**.

4. Sending of a **Final Notice before seizure**, indicating that the CIR is giving the taxpayer "the LAST OPPORTUNITY to settle the assessment".

5. Sending of a **Demand letter**, containing a text with the words "final decision" and "appeal"

6. **Referral** by the Commissioner of the request for reinvestigation to the Solicitor General because this shows the insistence of the Commissioner to collect tax.

7. Service of a **Preliminary Collection Letter**, since it presupposes the existence of a valid assessment notice.

b. Remedies of the Taxpayer in case the CIR Denies the Protest or Fails to Act on the Protest

In Case of Denial of Protest

Taxpayer may appeal to the CTA within **30 days from the date of receipt of the said decision**. (*R.A. No. 1125 as amended by R.A. No. 9282*)

In Case the Protest is not acted upon by the CIR or his authorized representative:

The taxpayer may either:

i. File a petition for review before the Court of Tax Appeals Division within thirty (30) days from the expiration of the 180-day period fixed by law for the Commissioner of Internal Revenue or his duly authorized representative to act on the disputed assessment; or

ii. Await the final decision of the Commissioner of Internal Revenue on the disputed assessment and appeal such final decision to the Court of Tax Appeals within thirty (30) days from the receipt thereof. This is true even if the

180-day period for the Commissioner to act on the disputed assessment had already lapsed.

These options are mutually exclusive and resort to one bars the application of the other. (*Light Rail Transit Authority vs. BIR, G.R. No. 231238, June 20, 2022*)

c. Effect of Failure to Appeal

The taxpayer's failure to appeal to the CTA in due time makes the assessment in question final, executory and demandable. Thus, when the action for collection is instituted, the taxpayer is already barred from disputing the correctness of the assessment or invoking any defense that would reopen the question of its tax liability on the merits. (*Republic vs. Lim Tian Teng, G.R. No. L-21731, March 31, 1966; Republic vs. CA, G.R. No. L-38540, April 30, 1987*)

iv. Compromise and Abatement of Taxes

Definition of Compromise

Contract between the government and the taxpayer to settle the liability.

Compromise as the amount paid by the taxpayer to settle his liability is different from compromise penalty which the amount paid by the taxpayer to compromise tax violation and paid in lieu of criminal prosecution.

Requisites for the compromise of taxes

1. Taxpayer has a liability

2. There must be an offer (by the taxpayer or Commissioner)

3. A reasonable doubt as to validity of claim against taxpayer exists or the financial position of the taxpayer demonstrates a clear inability to pay the assessed tax

4. There must be an acceptance (by the taxpayer or Commissioner, as the case maybe) of the offer in settlement of the original claim
Cases which could be subject to Compromise

ARELLANO UNIVERSITY SCHOOL OF LAW BAR OPERATIONS COMMISSION 2025

1. Delinquent accounts;
2. Cases under administrative protest after issuance of the FAN to the taxpayer which are still pending in the Regional Offices, Revenue District Offices, Legal Service, Large Taxpayer Service (LTS), Collection Service, Enforcement Service and other offices in the National Office;
3. Civil tax cases being disputed before the courts;
4. Collection cases filed in courts;
5. Criminal violations, other than those already filed in court or those involving criminal tax fraud. (*RR No. 30-2002*)

Cases that cannot be subject of compromise:

1. Withholding tax cases, unless the applicant taxpayer invokes provisions of law that cast doubt on the taxpayer's obligation to withhold;
2. Criminal tax fraud cases confirmed as such by the CIR or his duly authorized representative;
3. Criminal violations already filed in court;
4. Delinquent accounts with duly approved schedule of installment payments;
5. Cases where final reports of reinvestigation or reconsideration have been issued resulting in reduction in the original assessment and the taxpayer is agreeable to such decision by signing the required agreement form for the purpose.

On the other hand, other protested cases shall be handled by the Regional Evaluation Board (REB) or the National Evaluation Board (NEB) on a case to case basis;

6. Cases which become final and executory after final judgment of a court, where compromise is requested

on the ground of doubtful validity of the assessment; and

7. Estate tax cases where compromise is requested on the ground of financial incapacity of the taxpayer (*RR No. 30-2002*)

Authority of the CIR to Compromise Taxes

The CIR may compromise the payment of any internal revenue tax, when:

1. A reasonable doubt as to the validity of the claim against the taxpayer exists provided that the minimum compromise entered into is equivalent to 40% of the basic tax (**Doubtful Validity Test**);
2. The financial position of the taxpayer demonstrates a clear inability to pay the assessed tax provided that the minimum compromise entered into is equivalent to 10% of the basic assessed tax (**Financial Incapacity Test**)

Minimum Compromise Rates:

DOUBTFUL VALIDITY	FINANCIAL INCAPACITY
40% of the basic assessed tax	10% of the basic assessed tax

Where the basic tax involved exceeds P1,000,000.00 or the settlement offered is less than the prescribed minimum rates, the compromise shall be subject to the approval of the Evaluation Board composed of the Commissioner and the four (4) Deputy Commissioners. (*RR No. 9-2013*)

Definition of Abatement

An abatement is a diminution or decrease in the amount of tax imposed such that to abate is to nullify or reduce in value or amount.

Grounds:

1. The tax or any portion thereof appears to have been unjustly or excessively assessed; or

ARELLANO UNIVERSITY SCHOOL OF LAW BAR OPERATIONS COMMISSION 2025

2. The administration and collection costs involved do not justify collection of the amount due

Distinguish Compromise from Abatement of Taxes

COMPROMISE	ABATEMENT
Involves a reduction of the taxpayer's liability through a mutual agreement.	Involves the cancellation of the entire tax liability of a taxpayer.
Authorized Officer: CIR, REB, NEB	Authorized Officer: is only the CIR
Grounds are: 1. Reasonable doubt as to the validity of assessment; 2. Financial incapacity of the taxpayer	Grounds are: 1. The tax or any portion thereof appears to be unjustly or excessively assessed; or 2. Administration and collection costs involved do not justify the collection of the amount due

v. Recovery of Tax Erroneously or Illegally Collected

a. Grounds, Requisites, and Period for Filing a Claim for Refund or Issuance of a Tax Credit Certificate

Procedures for claiming refunds of tax erroneously or illegally collected under Section 229, NIRC, as amended:

1. A written claim for refund must be filed with the Commissioner within two years from the date of payment of the tax; (*Section 204, NIRC, as amended*)
2. The Commissioner shall process and decide the claim for refund under within one hundred eighty (180) days from the date of submission of complete documents in support of the

application filed. Should the Commissioner deny, in full or in part, the claim for refund, the Commissioner shall state the legal and/ or factual basis for the denial; (*Id.*)

3. In case of full or partial denial of the claim for credit/ refund, the taxpayer affected may, within thirty (30) days from the receipt of the decision denying the claim, appeal the decision with the Court of Tax Appeals (CTA); (*RR No. 5-2024*)
4. In case the tax refund/credit is not acted upon by the Commissioner within the 180-day period, the taxpayer-claimant may opt to: (i) Appeal to the CTA within the 30-day period after the expiration of the 180 days required by law to process the claim; or (ii) forego the judicial remedy and await the final decision of the Commissioner on the application of refund claim.

When the BIR failed to render a decision within the 180-day period and the taxpayer-claimant opted to seek for a judicial remedy within thirty (30) days from such period, the administrative claim for refund shall be considered moot and shall no longer be processed. (*RR No. 5-2024*)

Grounds for claim for refund and tax credit:

1. Tax is erroneously or illegally assessed or collected;
2. Penalty is imposed without authority;
3. Sum collected is excessive or in any manner wrongfully collected.

Distinguish Illegally collected tax from Erroneously collected tax

Illegally collected tax	Erroneously collected tax
There is a violation of certain provisions of tax law or statute.	There is a mistake in collection, not a

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Illegally collected tax	Erroneously collected tax
	violation of tax law/statute
The tax was paid by him under duress.	The payment was made under a mistake of fact.
The tax was collected in patent disregard of the law	The collection was made based on a misapplication of the law.

Distinguish Tax Refund under Section 229 and Section 112, NIRC, as amended

Section 229	Section 112
Tax Sought to be refunded	
Excessively or erroneously collected internal taxes	Excess input tax attributable to zero-rated sales
Reckoning Point of the 2-year period for claiming refund	
From the date of payment of the sought to be refunded	From the close of the taxable quarter when the relevant zero-rated sales were made
Period of time for the BIR to decide on the administrative claim	
Within 180 days from date of submission of the complete documents in support of the application filed	Within 90 days from the date of submission of the official receipts or invoices and other documents in support of the application of refund.

b. Proper Party to File Claim for Refund or Tax Credit

The NIRC, particularly Sections 204(C) and 229, provides the basis for a taxpayer's right to claim a refund or tax credit for taxes that were erroneously or illegally collected. These provisions state that a taxpayer may file a claim with the BIR to recover such taxes.

The proper party to question or seek a refund of an indirect tax is the statutory taxpayer, the person on whom the tax is

imposed by law and who paid the same even if he shifts the burden thereof to another. In this case, Petron is the statutory taxpayer. (*Silkair (Singapore), Pte. Ltd. vs. CIR, G.R. No. 174594, February 06, 2008*)

f. Government Remedies

i. Administrative Remedies

a. Tax Lien

Definition of Tax Lien

A charge on **all leviable property of the taxpayer** to secure the proper payment of the tax, surcharges, interests and costs.

Enforceable against all property and rights to property belonging to the taxpayer, and retroacts to the time when the tax assessment was made. (*Section 219, NIRC, as amended*)

Superior to all liens, charges or encumbrances in favor of any person.

Enforceable by administrative or judicial action, and may only be extinguished upon payment of the tax and the related interests and expenses. (*Section 257, LGC*)

b. Distraint and Levy

Definition of Distraint

Seizure of **personal property**, tangible or intangible, of a taxpayer to enforce the collection of delinquent taxes.

a. Actual - **physical seizure** of personal property of taxpayer (*Section 207, NIRC, as amended*)

b. Constructive - **personal property** is in control and supervision of government on the following cases (*Section 206, NIRC, as amended*)

i. is retiring from any business subject to tax, or

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- ii. is intending to leave the Philippines or to remove his property therefrom or
- iii. to hide or conceal his property or
- iv. to perform any act tending to obstruct the proceedings for collecting the tax due or which may be due from him.

Definition of Levy

Levy of real property refers to the same act of seizure as in distraint, but in this case, of real property, an interest in or rights to such property in order to enforce the payment of taxes. *(Section 207, NIRC, as amended)*

c. Forfeiture of Real Property

An administrative proceeding initiated by the BIR against a delinquent taxpayer in cases:

1. there is no bidder for real property exposed for sale or
2. if the highest bid is for an amount insufficient to pay the taxes, penalties a costs

d. Suspension of Business Operation

The Commissioner or his authorized representative is hereby empowered to suspend the business operations and temporarily close the business establishment of any person:

1. If, in the case of VAT-registered person, there's:
 - a. Failure to issue receipts or invoices;
 - b. Failure to file a VAT return as required under Section 114; or,
 - c. Understatement of taxable sales or receipts by thirty percent (30%) or more of his correct taxable sales or receipts for the taxable quarter.
2. Failure of any Person to Register as Required under Section 236.

The temporary closure of the establishment shall be for the duration of not less than five (5) days and shall be lifted only upon compliance with whatever

requirements prescribed by the CIR in the closure order. *(Section 115, NIRC, as amended)*

ii. Judicial Remedies

a. Civil Action

Under Republic Act No. 1125, as amended, and the 2005 Revised Rules of the CTA, as amended, the CTA Division shall exercise:

(i) Exclusive original over or appellate jurisdiction to review by appeal the following:

1. Decisions of the Commissioner of Internal Revenue in cases involving disputed assessments, refunds of internal revenue taxes, fees or other charges, penalties in relation thereto, or other matters arising under the National Internal Revenue Code or other laws administered by the Bureau of Internal Revenue;
2. Inaction by the Commissioner of Internal Revenue in cases involving disputed assessments, refunds of internal revenue taxes, fees or other charges, penalties in relation thereto, or other matters arising under the National Internal Revenue Code or other laws administered by the Bureau of Internal Revenue, where the National Internal Revenue Code provides a specific period for action, in which case the inaction shall be deemed a denial;
3. Decisions, orders or resolutions of the Regional Trial Courts in local tax cases originally decided or resolved by them in the exercise of their original jurisdiction;
4. Decisions of the Commissioner of Customs in cases involving liability for customs duties, fees or other money charges, seizure, detention or release of property affected, fines, forfeitures or other penalties in relation thereto, or other matters arising under the Customs Law or other laws administered by the Bureau of Customs;

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ARELLANO UNIVERSITY SCHOOL OF LAW BAR OPERATIONS COMMISSION 2025

5. Decisions of the Secretary of Finance on customs cases elevated to him automatically for review from decisions of the Commissioner of Customs which are adverse to the Government under Section 2315 of the Tariff and Customs Code;

6. Decisions of the Secretary of Trade and Industry, in the case of nonagricultural product, commodity or article, and the Secretary of Agriculture in the case of agricultural product, commodity or article, involving dumping and countervailing duties under Section 301 and 302, respectively, of the Tariff and Customs Code, and safeguard measures under Republic Act No. 8800, where either party may appeal the decision to impose or not to impose said duties; and

(ii) Exclusive jurisdiction over tax collection cases, to wit:

1. Original jurisdiction in tax collection cases involving final and executory assessments for taxes, fees, charges and penalties, where the principal amount of taxes and fees, exclusive of charges and penalties, claimed is One Million Pesos (P1,000,000.00) or more;

2. Appellate jurisdiction over appeals from the judgments, resolutions or orders of the Regional Trial Courts in tax collection cases originally decided by them within their respective territorial jurisdiction.

The apparent conflicting provisions of RA No. 9282 and BP. 129, as amended by RA No. 11576, are reconciled as follows:

- i. Exclusive original jurisdiction over tax collection cases involving P1,000,000.00 or more remains with the CTA;
- ii. Exclusive original jurisdiction over tax collection cases involving less than P1,000,000.00 shall be exercised by the proper first-level courts;
- iii. Exclusive appellate jurisdiction over tax collection cases originally decided by the first-level courts shall be exercised by the RTC;
- iv. Exclusive original jurisdiction over criminal offenses or felonies where the principal

amount of taxes and fees, exclusive of charges and penalties, claimed is P1,000,000.00 or more remains with the CTA;

- v. Exclusive original jurisdiction over criminal offenses or felonies where the principal amount of taxes and fees, exclusive of charges and penalties, claimed is less than P1,000,000.00 shall be exercised by the proper first-level courts; and (1) Exclusive appellate jurisdiction over criminal offenses or felonies originally decided by the first-level courts remains with the RTC.
- vi. It must be emphasized, however, that the foregoing clarification shall apply to cases filed upon the effectivity of RA No. 11576 on August 21, 2021 since jurisdiction over the subject matter in criminal cases is determined by the statute in force at the time of commencement of the action. *(People vs Mendez, G.R. Nos. 208310-11 & 208662, March 28, 2023)*

Mode of Appeals

Under Section 11 of Republic Act No. 1125, as amended, and the 2005 Revised Rules of the CTA, as amended, appeal to the CTA can be made as follows:

Who may File	Period to file an appeal
via Petition for Review under Rule 42 with the CTA Division	
A party adversely affected by the decision, ruling, or inaction of the: <ul style="list-style-type: none"> - Commissioner of Internal Revenue, - Commissioner of Customs, - Secretary of Finance, - Secretary of Trade and Industry - Secretary of Agriculture, - Regional Trial Court in the exercise of its original jurisdiction 	Within 30 days from receipt of the decision, ruling, or in case of inaction, from the expiration of the period fixed by law for an action or decision.
via Petition for Review under Rule 43 with the CTA En Banc	

DO NOT REPRODUCE

ARELLANO UNIVERSITY SCHOOL OF LAW BAR OPERATIONS COMMISSION 2025

Who may File	Period to file an appeal
A party adversely affected by the decision, ruling of the: 1. Central Board of Assessment Appeals; and 2. Regional Trial Court in the exercise of its appellate jurisdiction	Within 30 days from receipt of the decision or ruling.
via Petition for Review under Rule 43 with the CTA En Banc	
A party adversely affected by a decision or ruling of CTA Division on a motion for reconsideration or new trial.	Within 15 days from receipt of the decision or ruling.

Decisions which may be appealed to the CTA En Banc

- a. Decisions or resolutions on motions for reconsideration or new trial of the CTA in Divisions in the exercise of its exclusive appellate jurisdiction;
- b. Decisions, resolutions or orders of the RTCs in local tax cases decided or resolved by them in the exercise of their appellate jurisdiction;
- c. Decisions, resolutions or orders of the RTCs in tax collection cases decided or resolved by them in the exercise of their appellate jurisdiction;
- d. Decisions, resolutions or orders on motions for reconsideration or new trial of the CTA in Division in the exercise of its exclusive original jurisdiction over tax collection cases;
- e. Decisions of the CBAA in the exercise of its appellate jurisdiction over cases involving the assessment and taxation of real property originally decided by the provincial or city board of assessment appeals;
- f. Decisions, resolutions or orders on motions for reconsideration or new trial of the CTA in Division in the exercise of its exclusive original

jurisdiction over cases involving criminal offenses arising from violations of the NIRC or the Tariff and Customs Code and other laws administered by the BIR or BOC;

g. Decisions, resolutions or orders on motions for reconsideration or new trial of the CTA in Division in the exercise of its exclusive appellate jurisdiction over criminal offenses mentioned in the preceding subparagraph; and

h. Decisions, resolutions or orders of the RTCs in the exercise of their appellate jurisdiction over criminal offenses mentioned in subparagraph. (*Section 2 of Rule 4, Revised Rules of the Court of Tax Appeals*)

NOTE: The appeal to the CTA En Banc is proper only if it involves a final judgment or order. If what the taxpayer is assailing is an interlocutory order the proper remedy is filing a petition for certiorari under Rule 65 before the Supreme Court. (*Mendez vs. People, G.R. No. 179962, June 11, 2014*)

b. Criminal Action

Under Republic Act No. 1125, as amended, and the 2005 Revised Rules of the CTA, as amended, the CTA Division shall exercise exclusive jurisdiction over cases involving criminal offenses, to wit:

1. Original jurisdiction over all criminal offenses arising from violations of the National Internal Revenue Code or Tariff and Customs Code and other laws administered by the Bureau of Internal Revenue or the Bureau of Customs, where the principal amount of taxes and fees, exclusive of charges and penalties, claimed is one million pesos or more; and
2. Appellate jurisdiction over appeals from the judgments, resolutions or orders of the Regional Trial Courts in their original jurisdiction in criminal offenses arising from violations of the National Internal Revenue Code or Tariff and Customs Code and other laws administered by the Bureau of Internal Revenue or Bureau of Customs, where the principal amount of taxes and fees,

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exclusive of charges and penalties, claimed is less than one million pesos or where there is no specified amount claimed.

The institution of criminal action shall interrupt the running of the period of prescription. *(Section 2 of Rule 9, Revised Rules of the Court of Tax Appeals)*

All criminal actions shall be conducted and prosecuted under the direction and control of the public prosecutor. In criminal actions involving violation of the NIRC or other laws enforced by the BIR, and violations of the Tariff and Customs Code or other laws enforced by the BOC, the prosecution may be conducted by their respective duly deputized legal officers. *(Section 3 of Rule 10, Revised Rules of the Court of Tax Appeals)*

Period to Appeal decisions of RTC in criminal cases rendered in the exercise of its Original Jurisdiction

Filing a notice of appeal within 15 days from receipt of a copy of the decision or final order with the court which rendered the final judgment or order appealed from and by serving a copy upon the adverse party. *(Section 9 of Rule 9, Revised Rules of the Court of Tax Appeals)*

Period to Appeal decisions of RTC in criminal cases rendered in the exercise of its Appellate Jurisdiction

Appealed to the CTA En Banc by way of petition for review within 15 days from receipt of a copy of the decision or resolution appealed from. *(Section 9 of Rule 9, Revised Rules of the Court of Tax Appeals)*

Period to Appeal decisions of CTA division in criminal cases

Appealed by way of petition for review to the CTA en banc within 15 days from receipt of a copy of the decision or resolution appealed from. *(Section 9 of Rule 9, Revised Rules of the Court of Tax Appeals)*

a. Injunction Not Available to Restrain Collection

General rule: No court can issue an injunction to restrain collection of tax. *(Section 218, NIRC, as amended)*

Exception: When in the opinion of the CTA the collection of tax may jeopardize the interest of the government and/or the taxpayer, the CTA may suspend said collection and require the taxpayer to deposit the amount claimed or file a surety bond *(Section 11, R.A. No. 9282)*

CTA has the power to provide injunctive relief and dispense with the bond requirement in cases where the court determines that the method employed by the CIR in the collection of tax is not sanctioned by law. However, the CTA must preliminarily determine if the collection is compliant with the law. *(Sps. Pacquiao vs. CTA & CIR, G.R. No. 213394, April 6, 2016)*