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SyCipLaw TIPS

TAX ISSUES AND PRACTICAL SOLUTIONS

1. What are the rules on the exclusion of land in the computation of the PhP100 million threshold on total assets in order to qualify for the reduced corporate income tax rate of 20% under the CREATE Law?

The Bureau of Internal Revenue (*BIR*) has issued Revenue Memorandum Circular No. 62-2021 dated April 30, 2021 (*RMC No. 62-2021*) to clarify certain provisions of Revenue Regulations No. 5-2021 relative to corporate income taxation under Republic Act No. 11534, or the Corporate Recovery and Tax Incentives for Enterprises Act (*CREATE Law*). Section 27 (A) of the National Internal Revenue Code, as amended (*Tax Code*), and as amended further by the Create Law imposes an income tax rate of 25% on domestic corporations. However, a lower income tax rate of 20% is imposed on domestic corporations with net taxable income not exceeding PhP5 million and total assets not exceeding PhP100 million, excluding the land on which the particular business entity's office, plant and equipment are situated.

RMC No. 62-2021 makes the following clarifications on the exclusion of land in the computation of the PhP100 million threshold on total assets for a domestic corporation to qualify for the reduced corporate income tax (*CIT*) rate of 20%:

1. the value of the land to be used must be net of depreciation and allowance for bad debts;
2. the amount to be deducted may either be the cost of acquisition or the fair market value of the land, depending on which value is reflected in the financial statements;
3. the land whose value shall be excluded is limited to the particular land where the corporation's office, plant and equipment are situated during the taxable year in which the 20% CIT is imposed; the value of land held primarily for sale to customers or held for investment purposes, shall not be excluded in the determination of the corporation's total assets; and
4. in order to determine the value of the land that shall be excluded in the computation of total assets, the total value of the land shall be multiplied by the percentage of the floor area devoted to the corporation's office.

SyCipLaw TIP 1:
Domestic corporations that will apply the reduced CIT rate of 20% should ensure that they do not exceed the PhP100 million threshold on total assets. In computing the amount of total assets, they should take note of the rules on the exclusion of the amount of land in the computation (*i.e.*, net of depreciation and allowance for bad debts, use of cost of acquisition or fair market value, and limitations on which land is covered).

2. If the tax assessment is invalid, can a taxpayer still be convicted for willful failure to pay taxes?

No. In *People v. Cross Country Oil & Petroleum Corp., et al*. (CTA Crim. Case No. O-620, May 19, 2021), the accused corporation, as represented by its president and treasurer as its responsible officers, were charged with the crime of "willful failure to pay taxes on income tax" for taxable year 2009 under Section 255, in relation to Sections 253(d) and 256, of the Tax Code.

SyCipLaw Tip 2:
Taxpayers who are under prosecution for willful failure to pay any tax must examine the validity of the tax assessment. If the tax assessment is invalid, the taxpayer should not be considered to have willfully failed to pay the deficiency tax subject of the tax assessment.

The accused argued that the prosecution failed to prove that (a) the assessment for deficiency income tax made by the BIR was valid, and (b) the Final Decision on Disputed Assessment (*FDDA*) was served to and received by the accused. The accused argued that without receipt of the FDDA, the assessment could not have given rise to an obligation on the part of the accused to pay deficiency tax. Consequently, since the obligation pay the deficiency tax has not arisen, the accused cannot be held liable for willful failure to pay the said tax.

The Court of Tax Appeals (*CTA*) ruled that the prosecution failed to prove the guilt of the accused beyond reasonable doubt. According to the CTA, the prosecution must prove the following elements of willful failure to pay deficiency income tax: (a) the taxpayer is required under the Tax Code or its rules and regulations to pay the tax; (b) the taxpayer failed to pay the required tax at the time required by law or rules and regulations; and (c) the taxpayer willfully failed to pay the tax.

In this case, the CTA found that the first element is absent given that the assessment is invalid for the following reasons: (a) the Formal Letter of Demand and Final Assessment Notice (*FLD/FAN*) is void for failure to definitely set and fix the amount of income tax liability; (b) the FDDA is void for failure to state the facts and applicable law, rules and regulations, or jurisprudence on which the final decision is based; and (c) the prosecution failed to prove that the FDDA was actually received by the accused. Thus, in the absence of a valid assessment for deficiency tax, the first element of the crime charged is not present. Considering that the subject FLD/FAN and FDDA are void, the accused cannot be said to have failed to pay the deficiency income tax (second element), much more to have done so willfully (third element).

3. Can the Commissioner of Internal Revenue decide that a taxpayer is not entitled to an income tax holiday and assess deficiency income tax on this basis?

SyCipLaw Tip 3:
The determination of the BOI registration of a corporation, the corporation's entitlement to ITH, and the cancellation of the BOI registration of a corporation are all beyond the authority of the BIR.

No. In *Mindanao Mineral Processing Refining Corporation v. Commissioner of Internal Revenue* (CTA Case No. 9643, May 19, 2021), the Commissioner of Internal Revenue (*CIR*) assessed deficiency income tax against Mindanao Mineral Processing Refining Corporation (*Mindanao Mineral*) on, among other grounds, that Mindanao Mineral misrepresented the date of start of its commercial operations in 2009 and this misrepresentation caused the automatic cancellation of its Board of Investments (*BOI*) registration and entitlement to an income tax holiday incentive for fiscal year 2012.

The CTA ruled that the CIR has no power to cancel the registration or suspend the enjoyment of incentives of any BOI-registered enterprise for violation of the terms and conditions of its registration, since that power is explicitly vested in the BOI and such power may only be exercised after compliance with due process. The CTA explained that "[b]efore a registered enterprise is deprived of its ITH incentive, it is the BOI who must first exercise its quasi-judicial or administrative adjudicatory power over the case."

The CTA added that, in this case, not only was there an encroachment on the quasi-judicial or administrative adjudicatory power vested in the BOI, Mindanao Mineral was also deprived of due process since it was not given an opportunity to be heard before its registration was cancelled and its entitlement to income tax holiday voided.

The CTA also held that the CIR has no power to cancel Mindanao Mineral's BOI registration on the basis of the principle of piercing the veil of corporation fiction since it is the BOI which has the power to do so.

The CTA ruled that the CIR's act of declaring Mindanao Mineral's entitlement to an income tax holiday as having been voided is *ultra vires* as this power is reserved exclusively for the BOI. In this case, since there was no showing that the BOI cancelled Mindanao Mineral's BOI registration, it was still entitled to an income tax holiday.

SyCipLaw Tip 4:
Taxpayers should know the date of enactment of tax ordinances so that they can check whether the local government unit has the power and authority to enact a particular tax ordinance.

4. Given that a municipality cannot impose franchise taxes, can a municipal ordinance that imposed franchise taxes be cured by the subsequent conversion of a municipality into a city?

No. In *Manila Electric Co. v. City of Muntinlupa* (G.R. No. 198529, February 9, 2021), the Manila Electric Company (*MERALCO*) sought to invalidate Municipal Ordinance No. 93-35 of Muntinlupa, which imposed a franchise tax on public utilities. MERALCO argued that when the ordinance was passed on November 22, 1993, the City of Muntinlupa, which was then a municipality, did not have the power and authority to impose and collect a franchise tax.

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Muntinlupa was eventually converted into a city in 1995 under Republic Act No. 7926 otherwise known as An Act Converting the Municipality of Muntinlupa into a Highly Urbanized City to be known as the City of Muntinlupa (*RA 7926*), which provided that existing municipal ordinances shall continue to take effect within the City of Muntinlupa.

The Supreme Court ruled that the imposition of franchise taxes is evidently beyond the powers of a municipality under the Local Government Code. Muntinlupa being then a municipality when it enacted the franchise tax ordinance definitely had no power or authority to enact the same.

Furthermore, the Supreme Court ruled that RA 7926 did not cure the infirmity of the ordinance. Citing *City of Pasig v. Manila Electric Company* (G.R. No. 181710, March 7, 2018), the Supreme Court ruled that RA 7926 contemplates only those ordinances that are valid and legally existing at the time of their enactment. Consequently, RA 7926 did not cure the infirmity of franchise tax ordinance since an *ultra vires* ordinance is null and void and produces no legal effect from its inception.

5. Are the properties of the Metropolitan Waterworks and Sewerage System subject to real property taxes?

No, unless the beneficial use of the property has been extended to a taxable person. In *Metropolitan Waterworks and Sewerage System v. Central Board of Assessment Appeals* (G.R. No. 215955, January 13, 2021), the City Treasurer of Pasay sought to collect real property taxes from the Metropolitan Waterworks and Sewerage System (MWSS).

Citing the prior case of *MWSS v. The Local Government of Quezon City* (G.R. No. 194388, November 7, 2018), the Supreme Court noted that it had already settled with finality that MWSS is a government instrumentality vested with corporate powers and, as such, it is exempt from payment of real property taxes. In particular, the Supreme Court noted that, through Executive Order No. 596 and Republic Act No. 10149, or the GOCC Governance Act of 2011, the executive and legislative branches of government have both explicitly classified MWSS as a government instrumentality with corporate powers.

SyCipLaw Tip 5:
Note that while the liability for real property taxes generally rests on the owner of the real property at the time the tax accrues, this liability may be shifted to the beneficial user of the real property, such as when the property owned by the government is leased to private persons or entities.

As a government instrumentality, MWSS is exempt from real property taxes under Section 234(a) of the Local Government Code. However, this tax exemption ceases when the beneficial use of the real properties have been granted, for a consideration or otherwise, to a taxable person. In such a case, the liability to pay real property taxes devolves on the beneficial user. MWSS alleged that the beneficial user was Maynilad Water Services, Inc., pursuant to its concession agreement with MWSS. The Supreme Court, however, did not make any determination as to who the beneficial user was because of insufficiency of evidence.

6. What are the deadlines for the submission of the relevant reports and application form in connection with the Personal Equity and Retirement Account Act?

The Secretary of Finance has issued Revenue Regulations No. 6-2021 dated April 13, 2021 (*RR No. 6-2021*) to provide additional guidelines for the implementation of the tax provisions of Republic Act No. 9505, or the Personal Equity and Retirement Account Act of 2008 (*PERA Act*). This new issuance amends Revenue Regulations No. 17-2011.

SyCipLaw Tip 6:
Taxpayers should note the forms of the various PERA reports, which are attached as annexes to RR No. 6-2021. The form of the PERA-TCC is attached as Annex F to RR No. 6-2021.

RR No. 6-2021 provides the due dates for the submission of the following reports by the PERA Administrators:

1. Quarterly Report on PERA Contributions (Annex A of RR No. 6-2021) – due not later than the 15th day following the close of every quarter;
2. Quarterly Report on PERA Distributions/Early Withdrawals/Terminations (Annex B of RR No. 6-2021) – due within 60 days following the end of the quarter of the date of termination or withdrawal;
3. Annual Report on PERA Contributions (Annex C of RR No. 6-2021) – due within 60 days from the close of the calendar year;
4. Annual Report on PERA Distributions/Early Withdrawals/Terminations (Annex D of RR No. 6-2021) – due within 60 days from the close of the calendar year; an
5. Alphalist of PERA Contributors (Annex E of RR No. 6-2021) – due within 60 days from the close of the calendar year.

Under RR No. 6-2021, the application for a PERA-Tax Credit Certificate (*PERA-TCC*), which "refers to the document evidencing the amount of tax credit equivalent to five percent (5%) of the total amount of qualified PERA contributions made in a year," shall now be filed online thru the PERASys within 60 days from the close of the calendar year. All PERA-TCC are now readily accessible at the PERASys by the PERA Administrator for its issuance to their respective contributors and may be easily printed upon request of utilization by a qualified contributor.

A contributor may utilize the PERA-TCC "for the payment of income tax liabilities of qualified employee and self-employed contributors." For qualified overseas Filipino contributors, the PERA-TCC may be used in the payment of any internal revenue taxes. For employee contributors, "the PERA-TCC shall be submitted to the employer to apply the gross amount of the PERA-TCC in the annual-year adjustments for computing the net withholding tax due of the contributor-employee." In order to utilize the PERA-TCC, it must be surrendered and attached to the applicable tax returns to be submitted to the concerned Revenue District Office pursuant to the existing revenue guidelines and procedures.

7. What are the new excise tax rates on alcohol products, tobacco products, heated tobacco products, and vapor products?

The Secretary of Finance issued Revenue Regulations No. 7-2021 dated May 10, 2021 (*RR No. 7-2021*) which implements "the amendment of excise tax on alcohol and tobacco products, and the imposition of excise tax on heated tobacco products and vapor products" under Republic Act No. 11467 otherwise known as "An Act Amending Sections 109, 141, 142, 143, 144, 147,152, 263, 263-A, 265, and 288-A, and Adding a New Section 290-A to Republic Act No. 8424, as Amended, Otherwise Known as the National Internal Revenue Code of 1997, and For Other Purposes."

RR No. 7-2021 provides the revised rates and bases of excise taxes on alcohol products (*i.e.*, distilled spirits, wines, and fermented liquors) and cigars and cigarettes (distinguishing those packed by hand and by machine), and the new excise taxes on heated tobacco products and vapor products (*i.e.*, nicotine salt and conventional "freebase" or "classic" nicotine). RR No. 7-2021 indicates the date of effectivity or start date of the applicability of each of the rates.

SyCipLaw Tip 7:
Taxpayers should note the change in excise tax rates for alcohol products and cigars and cigarettes, as well as the newly imposed excise taxes on heated tobacco products and vapor products. Note that imprisonment and a fine that is 10 times the excise tax due are imposed as penalties for selling tobacco products, including heated tobacco products and vapor products, at a price lower than the combined excise and value-added taxes.

RR No. 7-2021 also provides the floor price or minimum price of cigarette, heated and vapor tobacco products, which "shall be the total production cost/expenses of the cheapest brand per tobacco product including the sum of excise tax and [value-added tax]." The BIR, through its Excise Large Taxpayer Regulatory Division, will establish a monthly data profile based on the required periodic manufacturer's or importer's sworn declaration for all brands per tobacco product category.

RR No. 7-2021 further provides the penalties for statutory offenses, including the selling of tobacco products at a price lower than the combined excise and value-added tax (*VAT*). Any person who sells tobacco products including heated tobacco products and vapor products at a price lower than the combined excise tax and VAT shall be punished with a fine of not less than 10 times the amount of excise tax, plus VAT due but not less than PhP200,000 nor more than PhP500,000, and imprisonment of not less than 4 years but not more than 6 years.