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1. Is there a deposit requirement for assailing the validity of an auction sale conducted by a local government to satisfy real property taxes?

Generally, yes.

Section 267 of the Local Government Code of 1991 (*LGC*) provides, in part, that "[n]o court shall entertain any action assailing the validity of any sale at public auction of real property or rights therein under this Title until the taxpayer shall have deposited with the court the amount for which the real property was sold, together with interest of two percent (2%) per month from the date of sale to the time of the institution of the action."

In *Province of Bataan, et al. v. Hon. Escalada, Jr., et al.* (G.R. No. 181311, November 24, 2021), the Supreme Court noted that: (1) the requirement for a deposit is jurisdictional and is an ingenious legal device to guarantee the satisfaction of the tax delinquency, with the local government unit keeping the payment on the bid price no matter the final outcome of the suit to nullify the tax sale; (2) the requirement only applies to initiatory actions and does not apply to the government or any of its agencies, especially when it is acknowledged to be tax-exempt; and (3) the requirement for a deposit is jurisdictional only if the tax delinquency of the real property is not disputed. It ruled that the taxpayer in said case should have made a deposit pursuant to Section 267 of the LGC considering that: (1) it filed a petition for injunction to declare the auction sale void on the ground that it was not duly notified of it; (2) it did not refute having any outstanding liability for real property taxes; and (3) it is not part of the government or a tax-exempt entity.

SyCipLaw TIP 1:

In deciding to challenge the validity of an auction sale conducted by a local government unit, the taxpayer must check whether the deposit requirement under Section 267 of the LGC applies (considering the nature of the action, whether the taxpayer enjoys any exemption, and whether tax delinquency is at issue). Unless the deposit requirement does not apply, the taxpayer must ensure that the deposit is paid given that the requirement is jurisdictional in nature, which means that the case may be dismissed for failure to comply.

2. What is the effect of the failure to strictly comply with the requisites for a public auction sale under the LGC?

Failure to strictly follow the requirements for an auction sale under Section 260 of the LGC renders the auction sale null and void.

In *Province of Bataan, et al. v. Hon. Escalada, Jr., et al.* (G.R. No. 181311, November 24, 2021) the Supreme Court ruled that the auction sale conducted by the Province of Bataan was null and void for non-compliance with certain requirements under Section 260 of the LGC. First, having been declared in default, the Province of Bataan failed to prove compliance with the requirements for a notice of sale (*i.e.*, that it posted a notice of sale at the main entrance of the provincial, city or municipal building and in a publicly accessible and conspicuous place in the barangay where the real property is located, and that it published the notice once a week for two weeks in a newspaper of general circulation in the province, city or municipality where the real property is located).

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Second, the auction sale sold more property than what was necessary or permissible under Section 260, which directs the auction of the property "or a usable portion thereof as may be necessary to satisfy the tax delinquency and expenses of sale." The Supreme Court said that the Province of Bataan should not have sold the machineries and equipment located on the real property since the value of the two parcels of land was already more than sufficient to satisfy the delinquent tax liability and expenses of the sale.

SyCipLaw TIP 2:

A taxpayer whose real property is levied upon and sold to satisfy delinquent real property taxes must check if the requirements for a valid auction sale under the LGC were strictly complied with by the local government unit. Failure to comply with the requirements may be cited as a ground to challenge the validity of the auction sale.

The Supreme Court explained that "strict adherence to the statutes governing tax sales is imperative not only for the protection of the taxpayers, but also to allay any possible suspicion of collusion between the buyer and the public officials called upon to enforce the laws. Failure to comply with these requisites shall render the tax sale null and void."

3. Is there a required period between filing an administrative claim and a judicial claim for refund of erroneously/illegally collected taxes under Sections 204 and 229 of the National Internal Revenue Code of 1997, as amended?

No. In *Commissioner of Internal Revenue v. Carrier Air Conditioning Philippines, Inc.* (G.R. No. 226592, July 27, 2021), the Supreme Court *En Banc* rejected the argument that the judicial claim for refund, which was filed only 10 days after the filing of the administrative claim for refund, was premature and violative of the doctrine of exhaustion of administrative remedies. Following its previous ruling in the 2015 case of CBK Power Company Limited v. Commissioner of Internal Revenue (where the judicial claim was filed merely 5 days after the administrative claim was filed), it reiterated the rule that as long as the administrative and judicial claims fall within the two-year period, there is no judicial impediment to the judicial claim for refund.

The Supreme Court explained that Sections 204 and 229 of the National Internal Revenue Code, as amended (*Tax Code*) require only that the administrative claim for refund be filed before the judicial claim for refund and that both the administrative and judicial claims for refund be filed within two years from the payment of the tax. From the plain language of the law, it does not matter how far apart the administrative and judicial claims were filed, or whether the Commissioner of Internal Revenue was actually able to rule on the administrative claim, so long as both claims were filed within the two-year prescriptive period.

SyCipLaw TIP 3:

A taxpayer seeking a refund of erroneously or illegally collected taxes must make sure that both its administrative and judicial claims for refund are filed within the two-year prescriptive period, even if the Commissioner of Internal Revenue fails to act on its claim.

The Supreme Court observed that the lack of a specific period fixed by the law within which the Commissioner must decide the refund claim has at times led to delays (to the taxpayer's prejudice) or to instances where the Commissioner was deprived of the opportunity to act on the matter because of the short interval between the filing of the administrative and judicial claims. However, the Supreme Court said that "[n]onetheless, the silence or insufficiency of the law on the reasonable period for the Commissioner's action is one that can be addressed not by judicial pronouncement, but by appropriate legislation."

4. Is a tax assessment valid absent a Letter of Authority and the Bureau of Internal Revenue conducting its own examination of the taxpayer's books of accounts and other accounting records?

No. In *Commissioner of Internal Revenue v. Pueblo De Oro* (CTA EB No. 2303 [CTA Case No. 9533], April 18, 2022), the Court of Tax Appeals (*CTA*) ruled that an assessment issued by the Bureau of Internal Revenue (*BIR*) without conducting an examination of the taxpayer's books of accounts and other accounting records, but simply based on a letter issued by the Board of Investments (*BOI*) to the BIR is a void assessment.

In this case, the taxpayer argued that the deficiency income tax assessment issued against it is not valid since no Letter of Authority (*LOA*) was issued by the BIR. The tax assessment was based solely on the findings of the BOI instead of the BIR conducting an independent investigation of the taxpayer's books of accounts and other accounting records.

The BIR, on the other hand, argued that under Section 5 of the Tax Code, the BIR is empowered to ascertain the correctness of a tax return in order to determine any liability for an internal revenue tax. It asserted that, because the deficiency tax assessment did not emanate from the examination of the taxpayer's books of accounts and other accounting records, but from a letter of the BOI to the BIR informing the latter of the denial of the taxpayer's request for an income tax holiday, an LOA is not needed.

SyCipLaw TIP 4:

Taxpayers should insist on their right to an independent investigation and examination of the facts that would justify the issuance of a deficiency tax assessment. A tax assessment based on the findings of a different government agency is not a sufficient basis for a tax assessment.

A motion for reconsideration of the decision is currently pending.

CTA decisions, while persuasive, do not become the law of the land, unlike decisions of the Supreme Court.

The CTA disagreed with the BIR and ruled that, by making such an assertion, the BIR had in effect admitted that it did not conduct an independent investigation and examination of the facts that would justify the issuance of a deficiency tax assessment.

The CTA ruled that, in the issuance of a tax assessment, the BOI's findings cannot serve as a substitute for an actual examination and investigation that the BIR should have conducted to ascertain the amount of the taxpayer's tax liability. According to the CTA, by merely adopting the BOI's findings as its basis for issuing a deficiency tax assessment against the taxpayer without verifying the same, the BIR violated the taxpayer's right to due process.

5. What is the *Origin of the Claim Test* in Taxation?

The *origin of the claim test* is based on US jurisprudence, in particular, *U.S. v. Gilmore* (372 U.S. 39, February 18, 1963). The test provides that in characterizing claims for taxation, the origin and character of the claim with respect to which an expense was incurred or a gain realized, rather than its potential consequences upon the fortunes of the taxpayer, is the controlling test.

The CTA recently applied the *origin of the claim test* in resolving *Commissioner of Internal Revenue v. Emmanuel C. Onate* (CTA EB No. 2370 [CTA Case No. 9498], March 18, 2022). One of the issues in the case is whether the monetary award received by the respondent from a final and executory judgment against a bank, arising from undocumented withdrawals from his trust accounts plus interest, is taxable as a judicial award or as long-term investments, if at all. The CTA applied the *origin of the claim test* to determine the origin and character of the judgment award.

In this case, the bank paid the judgment award to the respondent net of the 20% final withholding tax applicable to interest/yield from bank deposits/deposit substitutes, amounting to PhP25,702,952.11.

SyCipLaw TIP 5:

Taxpayers should keep in mind the *origin of the claim test* when opposing claims made by the BIR. The origin and character (e.g., whether income or capital, or whether personal or business expenses) of amounts received will determine whether such amounts are taxable income.

A motion for reconsideration of the decision is currently pending.

CTA decisions, while persuasive, do not become the law of the land, unlike decisions of the Supreme Court.

The respondent filed a written claim for refund or tax credit for the amount of PhP25,702,952.11, asserting that the interest subject of the case was interest on long-term investments that were wrongfully taken from his bank accounts and which interest is expressly exempt from income tax under the Tax Code. The BIR, on the other hand, argued that the interest subject of the case is not interest from a long-term investment, but interest from a judgment award, hence, subject to a final withholding tax. The CTA, in Division, ordered the refund or issuance of tax credit certificate in the amount of PhP25,702,952.11 in favor of the respondent and held that the legal interest imposed on the judgement award is not taxable.

The CTA *En Banc* affirmed the decision. Applying the *origin of the claim test*, the CTA *En Banc* ruled that the payments received by the respondent under the judgment award originated from the trust accounts he invested with the bank. Because the Supreme Court ordered the bank to return the undocumented withdrawals from the trust accounts, those funds are merely a return of capital to the taxpayer. Furthermore, with respect to the interest that were also awarded with the restored funds, they are in the nature of an indemnity to the respondent for the income he could have earned from the funds had they not been debited by the bank. If the funds that were returned to the respondent had only remained in the trust accounts with the bank, they would have earned interest income that is expressly exempt under the Tax Code because they qualify as long term investments.

6. What is *e-Sabong* and how is it taxed?

Electronic Sabong or e-Sabong is the online and/or remote or off-site wagering/betting on live cockfighting matches, events, and/or activities streamed or broadcasted live from cockpit arenas that are licensed or authorized by the local government units having jurisdiction over such arenas. The Philippine Amusement and Gaming Corporation (*PAGCOR*) created the E-Sabong Licensing Department to exercise regulatory functions over e-Sabong operations and approved the Regulatory Framework for Electronic Sabong on April 27, 2022. However, upon the recommendation of the Department of Interior and Local Government, the President subsequently issued a verbal directive to halt all e-Sabong operations immediately. Consequently, PAGCOR has directed all licensed e-Sabong operators to shut down their gaming websites and cease all gaming operations accordingly.

Presidential Decree (*PD*) No. 1869, as amended by RA No. 9487, vested PAGCOR with the authority to license recreation or amusement places within the Philippines. PD No. 1869, as amended, provides that "no tax of any kind or form, income or otherwise, as well as fees, charges or levies of whatever nature, whether National or Local, shall be assessed and collected under this Franchise from [PAGCOR]; nor shall any form of tax or charge attach in any way to the earnings of [PAGCOR], except a Franchise Tax of five (5%) percent of the gross revenue or earnings derived by [PAGCOR] from its operation under this Franchise." Applying PD No. 1869, as amended, the Supreme Court, in Bloomberry Resorts and Hotel, Inc. v. BIR, held that similar to PAGCOR, PAGCOR's contractees and licensees remain exempt from the payment of corporate income tax and other taxes, except for the 5% franchise tax on their income from gaming operations. However, it was further clarified in Thunderbird Pilipinas Hotel & Resorts, Inc. v. CIR, that the value-added tax (*VAT*) exemption of PAGCOR extends only to entities that have contracted with PAGCOR in connection with their gaming operations and does not extend to licensees.

Prior to the suspension of e-Sabong operations, the BIR issued Revenue Memorandum Circular (*RMC*) No. 25-2022 to clarify the tax consequences arising from e-Sabong operations regulated by PAGCOR including digital transactions that are not clearly covered by existing tax regulations. The RMC made a distinction between "gaming income" or the percentage commission taken by the e-Sabong operator from the center or initial bet (*i.e.*, the amount of money gamecock owners wager on their own fighting cocks), and "service income" pertaining to the percentage commission obtained by the e-Sabong operator from the total gross sales or total bets for every cockfight in the "Meron", "Wala" and "Draw" sides, accepted through the e-Sabong betting portals, excluding the "center bets".

RMC No. 25-2022 provides that the gaming income from e-Sabong operations by an e-Sabong operator is subject to a five percent (5%) franchise tax in lieu of all internal revenue taxes except VAT or percentage tax (depending on the threshold).

However, if the e-Sabong operator has contracted with PAGCOR for the provision of goods and services for PAGCOR's gaming operations, then its provision of goods and services to PAGCOR is subject to zero-rated VAT. This benefit, however, does not apply to the service income and other income from e-Sabong by an e-Sabong operator which are subject to regular income tax, VAT, or percentage tax, as well as applicable withholding taxes. If the e-Sabong operator is unauthorized, such operator will not be covered under the fiscal regime under the PAGCOR charter and will be subject to the appropriate taxes and penalties under the Tax Code, in addition to the penalties and sanctions that may be imposed by the appropriate regulatory government agencies.

SyCipLaw TIP 6:

While e-Sabong operations have been suspended pursuant to the directive of the President, e-Sabong operators who have earned income prior to the suspension of their operations must ensure that there is a clear distinction between gaming income, service income, and other income in its books to prevent assessments for deficiency taxes from the BIR, considering that only their gaming income is subject to five percent (5%) franchise tax in lieu of all other taxes.

7. Are amended tax returns subject to the 25% surcharge?

No, provided that the amendment was made to pay the correct tax and the original tax return was filed on or before the deadline.

Section 248 (A) of the Tax Code imposes a penalty equivalent to twenty-five percent (25%) of the amount of tax due when there is (i) failure to file any return and pay the tax due, (ii) a tax return is filed with the wrong internal revenue office, (iii) failure to pay the deficiency tax within the time prescribed for its payment in the notice of assessments, (iv) failure to pay the full or part of the amount of tax shown on any tax return required to be filed, or the full amount of the tax due for which no return is required to be filed, on or before the time prescribed for payment.

In RMC No. 43-2022, the BIR clarified that the 25% surcharge will not be imposed if the taxpayer amends its tax return to pay the correct tax due provided that the taxpayer was able to file the initial tax return on or before the prescribed due date for its filing. However, the 25% surcharge will be imposed on a tax deficiency discovered during a tax audit if the tax return being audited was filed beyond the prescribed period.

SyCipLaw TIP 7:

Taxpayers should ensure that completed tax returns are filed (and the taxes due are paid) on or before the due date prescribed under the law. However, in case the taxpayer finds it necessary to file a subsequent amendment to its tax returns in order to reflect the correct taxes that are due, the taxpayer can now voluntarily amend the tax returns and pay the additional taxes due based on the amended tax returns (instead of waiting for a tax audit) since RMC No. 43-2022 has clarified that the 25% surcharge will not be imposed provided that the initial unamended tax return was filed on time.

In RMC No. 43-2022, the BIR clarified that the 25% surcharge will not be imposed if the taxpayer amends its tax return to pay the correct tax due provided that the taxpayer was able to file the initial tax return on or before the prescribed due date for its filing. However, the 25% surcharge will be imposed on a tax deficiency discovered during a tax audit if the tax return being audited was filed beyond the prescribed period.

RMC No. 43-2022 reconciled the provisions in RMC No. 54-2018 and RMC No. 46-1999 in relation to the imposition of the 25% surcharge. In RMC No. 54-2018, the BIR clarified that the 25% surcharge shall be imposed on the additional tax to be paid if a taxpayer amends its tax return and an additional tax is due based on the amended tax return. However, in RMC No. 46-1999, it was provided that the 25% surcharge will not be imposed in case of a deficiency tax assessment as a result of tax audit if the taxpayer filed its tax return on time. The BIR recognized that following the policy under RMC No. 54-2018 and RMC No. 46-1999 discourages taxpayers from voluntarily amending their tax returns to pay the correct tax due. Under the earlier RMCs, a taxpayer is unduly penalized for voluntarily amending its tax returns in order to pay the correct tax due but the taxpayer is unintentionally rewarded if it amends its tax returns in order to pay the correct tax as a result of a tax audit.

Accordingly, the new circular expressly provides that the 25% surcharge will not be imposed in case of an amendment of a tax return if the taxpayer was able to file the initial tax return on or before the prescribed due date for its filing, regardless whether the amendment of the tax return was done voluntarily or due to a tax audit.

8. What are the latest updates on the VAT rules under the Corporate Recovery and Tax Incentives for Enterprises Act and its implementing rules?

The BIR issued RMC No. 49-2022 to amend certain portions of RMC No. 24-2022 which clarified issues relative to Revenue Regulation (*RR*) No. 21-2021 and certain issues pertaining to the effectivity and VAT treatment of transactions by registered business enterprises (*RBEs*), particularly the registered export enterprises.

The issuance of RMC No. 49-2022 was in response to the request of taxpayers affected by the deferment of RR No. 9-2021, which provided for the imposition of 12% VAT on certain transactions that were taxed at zero percent (0%) VAT under the Tax Code, and to align RMC No. 24-2022 with the provisions of the Corporate Recovery and Tax Incentives for Enterprises (*CREATE*) Act and its implementing rules and regulations.

VAT sales during the deferment of RR No. 9-2021: Q&A No. 10

The BIR recognized that there are transactions other than the sales of goods and services to registered export enterprises and DMEs located in ecozones and freeport zones that may have been affected by the deferment of RR No. 9-2021. RMC No. 49-2022 confirmed that the non-retroactivity provision under Section 246 of the Tax Code will apply; thus, all transactions that have been treated by the seller as VAT zero-rated for the period July 1, 2021 to December 9, 2021 will remain VAT zero-rated, even if the transactions are not qualified for VAT zero-rating.

If the seller applied the 12% VAT to the said transactions, the seller has the option of retaining the 12% VAT declaration or reverting the transaction from VATable to VAT zero-rated.

Sale of goods and services by DMEs located in ecozones or freeport zones: Q&A No. 17

RMC No. 49-2022 clarified the VAT treatment of sales by registered non-export locators or domestic market enterprises (*DMEs*) located in ecozones and freeport zones depending on whether the sellers were registered prior to the CREATE Act or during its effectivity.

If the *seller is registered prior to the CREATE Act*, its sales of goods may be exempt from VAT, zero-rated or subject to VAT depending on the buyer of these goods and whether the seller is under the 5% Gross Income Tax (*GIT*) regime or under the income tax holiday (*ITH*). Below are the applicable VAT treatment:

1. **VAT Exempt** – Sales of DME-locators under the 5% GIT regime to the extent of their registered activity to enterprises inside the ecozones or freeport zones or from the customs territory.
2. **0% VAT** – Sales of DME-locators under the ITH regime to registered export enterprises provided that these goods are directly and exclusively used in the latter's registered activity.
3. **12% VAT** – Sales of DME-locators under the ITH regime to non-export locators or DMEs within the ecozones and freeport zones, and to enterprises from the customs territory.

If the *seller is registered during the effectivity of the CREATE Act*:

1. **0% VAT** - Sales to registered export enterprises provided the goods and services are directly and exclusively used in the registered project or activity.
2. **12% VAT** - Sales to DMEs within the ecozones and freeport zones, and to enterprises from the customs territory.

SyCipLaw TIP 8:

Non-export locators should be guided by the provisions of RMC No. 49-2022 in determining whether their sales of goods/services are VAT exempt, VAT zero-rated, or VATable. A distinction must be made between businesses that have registered prior to the CREATE Act and after its effectivity, since DMEs under the CREATE Act can no longer have sales that are exempted from VAT. Local suppliers of goods/services must note that prior approval from the BIR is necessary to validate whether the requisites are complied with before the availment of the zero-rating incentive by the supplier of the registered export enterprise. However, qualified sales transactions that occurred prior to the effectivity of RMC No. 49-2022 may not require prior application provided that the seller is still able to present the documents required by the BIR in the application for VAT zero-rating.

Change of registration from VAT to non-VAT: Q&A No. 31

Under RMC No. 24-2022, registered export enterprises shifting from the ITH to the 5% GIT or SCIT regime or already enjoying 5% GIT regime but are still VAT-registered at the time the CREATE Act took effect have two (2) months from the expiration of their ITH or the effectivity of RMC 24-2022, respectively, to change their registration status from a VAT-registered entity to non-VAT. However, RMC No. 49-2022 clarified that if the registered export enterprise has activities other than those registered with the IPA that are subject to VAT (i.e., VAT at l2% and 0%), it must remain a VAT taxpayer and report the sales in the VAT returns as VATable, zero-rated and/or VAT-exempt, as the case may be.

Prior approval for VAT zero-rating: Q&A No. 33

While RMC 24-2022 emphasized that the registered export enterprise's local supplier of goods/services should secure prior approval from the BIR for its sales to be accorded VAT zero-rating, RMC No. 49-2022 clarified that for sales transactions that are qualified for VAT zero-rating but the taxpayer failed to secure an approved application for VAT zero-rating with the BIR, prior application may not be required until March 9, 2022 (the date of effectivity of RMC No. 49-2022), provided the sellers have the following documents: (i) certificate of registration and VAT certification issued by the IPA where their export enterprise buyers are registered; (ii) sworn affidavit executed by the registered export enterprise-buyer, stating that the goods and/or services bought are directly and exclusively used for the production of goods and/or completion of services to be exported or for utilities and other similar costs, the percentage of allocation to be directly and exclusively used for the production of goods and/or completion of services to be exported; and (iii) other documents to corroborate entitlement to VAT zero-rating such as but not limited to duly certified copies of purchase order, job order or service agreement, sales invoices and/or official receipts, delivery receipts, or similar documents to prove existence and legitimacy of the transaction.