GENERAL PRINCIPLES OF TAXATION

Part Two

Atty. V. Salud, CPA, REB, REA

SITUS OF TAXATION

Situs of Taxation – Place of Taxation

The basic rule is that the state where the subject to be taxed has a situs may rightfully levy and collect the tax; and the situs is necessarily in the state which has jurisdiction or which exercises dominion over the subject in question.

Protection is the basic consideration that justifies situs of taxation.

SITUS OF TAXATION

Situs of Subjects of Taxation

1. Persons – A state may levy a personal tax upon persons (inhabitants or residents) subject of its sovereignty. E.g. community tax
2. Real property – taxable in the state in which it is located whether the owner is a resident or non-resident. (Rule of Lex Rei Sitae)
3. Tangible personal property – taxable in the state where it has actual situs or where it is physically located. (Lex Rei Sitae)
4. Intangible personal property – the general rule is that the situs is at the domicile of the owner in accordance with the principle of mobilia sequuntur personam.

   Exception: when it is consistent with express provisions of the statute or when justice does not demand that it should be, as where the property has in fact a situs elsewhere. E.g. shares of stock in a domestic corporation of a non-resident foreigners are taxable in the Philippines.

SITUS OF TAXATION

Situs of Subjects of Taxation

5. Income – factors that affect situs: a) citizenship or nationality of the person taxed; b) domicile or residence of the person taxed; and c) source of income taxed

Taxable Persons	Source of Income	
INDIVIDUALS	WITHIN THE PHILIPPINES	OUTSIDE THE PHILIPPINES
Resident Citizens	YES	YES
Non-resident Citizens	YES	NO
Resident Aliens	YES	NO
Non-Resident Aliens	YES	NO

SITUS OF TAXATION

Situs of Subjects of Taxation

6. Business, occupations and transactions – situs is the place where the business is done, or the occupation is engaged in, or the transaction took place. E.g. VAT, percentage tax

7. Gratuitous transfer property – factors that affect situs: a) citizenship or nationality of the donor or deceased; b) domicile or residence of the donor or deceased; and c) place where the property is located. E.g. estate tax, donor's tax

SITUS OF TAXATION

Situs of Subjects of Taxation

Taxable Persons	Source of Income	
CORPORATIONS	WITHIN THE PHILIPPINES	OUTSIDE THE PHILIPPINES
Domestic Corporations	YES	YES
Resident Foreign Corporations	YES	NO
Non-resident Foreign Corporations	YES	NO

SITUS OF TAXATION

Situs of Subjects of Taxation

ESTATE TAX & DONOR'S TAX	Location of the Property	
DONOR OR DECEASED	IN THE PHILIPPINES	OUTSIDE THE PHILIPPINES
Resident Citizen	YES	YES
Non-Resident Citizen	YES	YES
Resident Alien	YES	YES
Non-resident Alien	YES	NO

DOUBLE TAXATION

Double Taxation

- taxing the same property twice when it should be taxed but once.
- taxing the same person twice by the same jurisdiction over the same thing.

DOUBLE TAXATION

Kinds of Double Taxation

1. Direct duplicate taxation – double taxation in the objectionable or prohibited sense (obnoxious).

   Two taxes must be imposed:

   a. on the same subject matter
   b. for the same purpose
   c. by the same taxing authority
   d. within the same jurisdiction
   e. during the same taxing period
   f. of the same kind or character

DOUBLE TAXATION

E.g.

The taxpayer was being required to pay two taxes under Manila City Tax Ordinance No. 7794, namely:

Sec. 14 – Tax on Manufacturers, Assemblers and Other Processors

Sec. 21 – Tax on Businesses Subject to Excise, VAT or Percentage under the National Internal Revenue Code

Issue: Is there double taxation?

DOUBLE TAXATION

Held: Yes, there is indeed double taxation. The taxpayer is subjected to the taxes under both Sections 14 and 21 of the Tax Ordinance No. 7794, since these are being imposed:

a. on the same subject matter – the privilege of doing business in the City of Manila

b. for the same purpose – to make persons conducting business in the City if Manila contribute to city revenues

c. by the same taxing authority – City of Manila

d. within the same jurisdiction – within the territorial jurisdiction of the City of Manila

e. during the same taxing period – per calendar year

f. of the same kind or character – local business tax imposed on gross sales or receipts of business.

(City of Manila vs. Coca-Cola Bottlers Philippines, Inc., G.R. No. 181845, August 4, 2009)

DOUBLE TAXATION

Kinds of Double Taxation

2. Indirect duplicate taxation (Broadest sense) – double taxation other than direct duplicate. It extends to all cases in which there is a burden of two or more pecuniary impositions. The absence of any one of the elements of direct duplicate taxation will make it indirect duplicate taxation which is not legally objectionable.

   E.g.

   a. Taxes imposed upon same property by 2 different states (International double taxation)

   b. Taxes imposed upon same income by 2 different states (international double taxation)

   c. Taxes imposed upon sales by the local government and national government (domestic double taxation)

DOUBLE TAXATION

Means Employed to Avoid or Minimize the Harsh Effects of Double Taxation

1. Tax Credit – amount that can be deducted from tax due in order to get the tax still due or payable. E.g. foreign income tax paid may be claimed as a tax credit against Philippine income tax due.
2. Tax deduction – amount that can be subtracted from gross income in order to arrive at taxable income. E.g. foreign income tax paid may be claimed as a tax deduction instead of tax credit.
3. Tax exemption – immunity from taxation to which others are subjected. E.g. Under the Tax Code, income earned from outside the Philippines by a non-resident citizen is not subject to Philippine income tax
4. Tax treaty with other states – entered into to reconcile the national fiscal legislations of the contracting parties and in turn help the taxpayer avoid simultaneous taxations in two different jurisdictions (international double taxation).

DOUBLE TAXATION

Illustration:

The domestic corporation had the following data for taxable year 2019:

	Philippines	Country X
Gross Income	P20,000,000	P10,000,000
Deductions	P7,000,000	P3,00,0000
Income tax paid		P1,750,000

DOUBLE TAXATION

	Foreign Income Tax not claimed as Tax Credit or Tax Deduction	If Foreign Income Tax is claimed as Tax Deduction	If Foreign Income Tax is claimed as Tax Credit
Gross Income	P30,000,000	P30,000,000	P30,000,000
Less: Deductions	10,000,000	10,000,000	10,000,000
Foreign Income Tax	0	1,750,000	0
Taxable Income	P20,000,000	P18,250,000	P20,000,000
Philippine Income Tax Due at 30%	P6,000,000	P5,475,000	P6,000,000
Less: Tax Credit (Foreign Income Tax)	0	0	1,750,000
Philippine Income Tax Still Due or Payable	P6,000,000	P5,475,000	P4,250,000

FORMS OF ESCAPE FROM TAXATION

No Loss of Revenue to Government

- Shifting
- Capitalization
- Transformation

Resulting in Loss of Revenue

- Evasion
- Avoidance
- Exemption

FORMS OF ESCAPE FROM TAXATION

Forms of Escape From Taxation

Shifting – is the transfer of tax burden by the statutory taxpayer (impact of taxation) to another or someone else (incidence of taxation).

Relations among Impact, Shifting and Incidence

- Impact of Taxation – point on which tax is originally imposed. (Initial phenomenon)
- Shifting – immediate process
- Incidence of Taxation – point on which the tax burden finally rests or settles down. (Result)

FORMS OF ESCAPE FROM TAXATION

Forms of Escape From Taxation

Kinds of Shifting

- Forward shifting- when tax burden is transferred from a factor of production through the factors of distribution until it finally settles on the ultimate purchaser or consumer.

  E.g. From Retailer to Consumer, the gross selling price of the goods is P100,000. The buyer who absorbs the VAT will pay P112,000 since the VAT is P12,000

- Backward shifting- when tax burden is transferred from consumer through factors of distribution to the factors of production.
  - E.g. From Consumer to Retailer, the amount to be paid by the buyer is just P100,000 and not P112,000. In this case, the retailer absorbs the VAT which is P10,714.29 (P100,000/1.12 x 12%)

FORMS OF ESCAPE FROM TAXATION

Forms of Escape From Taxation

Kinds of Shifting

- Onward shifting- when the tax is shifted two or more times either forward or backward

  E.g. From manufacturer to retailer to ultimate consumer.

FORMS OF ESCAPE FROM TAXATION

Forms of Escape From Taxation

Capitalization

- A reduction in the price of the taxed object equal to the capitalized value of future taxes which the purchaser expects to be called upon to pay.

E.g. The selling price of the real property is P1,000,000 and the real property tax thereon for five years is P50,000. If the buyer pays P950,000 only, the seller in effect shoulders the real property tax burden of the buyer.

FORMS OF ESCAPE FROM TAXATION

Forms of Escape From Taxation

Transformation – the manufacturer or producer upon whom the tax has been imposed, fearing the loss of his market if he should add the tax to the price, pays the tax and endeavors to recoup himself by improving his process of production, thereby turning out his units at a lower cost.

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Illustration:	**Reduced Sales**	**Reduced Profit**	**Transformation**
Selling Price	P850	P850	P850
Add'l Selling Price Representing Excise Tax Passed on to Buyer	150	0	0
Cost of Production	(600)	(600)	(450)
Excise Tax	(150)	(150)	(150)
Profit	P250	P100	P250

FORMS OF ESCAPE FROM TAXATION

Tax Evasion – the use by the taxpayer of illegal means to defeat or lessen the payment of tax.

Factors in Tax Evasion

- The end to be achieved
- An accompanying state of mind which is evil, in bad faith, willful or deliberate and not accidental
- A course of action or failure of action which is unlawful

FORMS OF ESCAPE FROM TAXATION

E.g. Substantial underdeclaration of sales, receipts or income or

Substantial overstatement of deductions

Substantial underdeclaration or overstatement

– more than 30% of the declared or reported sales, receipts or income , or

- more than 30% of the actual deductions.

FORMS OF ESCAPE FROM TAXATION

Tax Avoidance – 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. interest derived from bank deposit

if savings deposit, the interest is subject to 20% final tax

if time deposit with maturity of not less than 5 years – tax-exempt

sale of shares of stock in a domestic corporation

thru the stock exchange – subject to stock transaction tax of 6/10 of 1% of the gross selling price

not thru the stock exchange – subject to capital gains tax of 15% on the capital gain

CAPITAL GAINS TAX vs. STOCK TRANSACTION TAX (TAX AVOIDANCE)

	All individuals and DC		All individuals And DC	
Selling Price	P2,000,000		P6,000,000	
Cost	(1,500,000)		(7,000,000)	
Capital Gain (Loss)	P500,000		(P1,000,000)	
Capital Gains Tax (if sold not thru the stock exchange)	P75,000		P0	Better option, the taxpayer will have a tax savings of P36,000
Stock Transaction Tax (if thru stock exchange)	P12,000	Better option, the taxpayer will have a tax savings of P63,000	P36,000	

FORMS OF ESCAPE FROM TAXATION

Distinctions between Tax Evasion and Tax Avoidance

- As to Validity
  - Tax evasion is illegal and subject to criminal penalty
  - Tax avoidance is legal and thus not subject to criminal penalty
- As to Effect
  - Tax evasion results in absence of taxation
  - Tax avoidance results in tax minimization

FORMS OF ESCAPE FROM TAXATION

Tax Exemption– grant of immunity to particular persons or corporations from tax persons and corporations generally within the same state or taxing district are obliged to pay.

E.g. Exemptions under the Constitution, Tax Code and Special laws

Nature of Power to Grant Tax Exemption

1. National Government – Inherent as power to tax implies the power to prescribe who or what shall not be taxed.
2. Local Governments – don't have the inherent power to exempt from taxation

FORMS OF ESCAPE FROM TAXATION

Grounds for Tax Exemption

1. Based on Contract – government is supposed to receive a full equivalent therefor.
2. Based on Some Ground of Public Policy – gov't need not receive any consideration in return for the tax exemption.
3. Created in a Treaty on Grounds of Reciprocity – to lessen the rigors of international double or multiple exemption.

Nature of Tax Exemption

1. It is a mere personal privilege of the grantee.
2. It is generally revocable by the government unless the exemption is founded on a contract.
3. It implies a waiver on the part of the Government of its right to collect. Hence, it exists only by virtue of an express grant and must be strictly construed.
4. It is not necessary discriminatory so long as the exemption has a reasonable foundation or rational basis.

FORMS OF ESCAPE FROM TAXATION

Kinds of Tax Exemption

1. As to Manner of Creation
   a. Express or affirmative exemption – when certain persons, property or transactions are, by express provision, exempted from all or certain taxes like exemptions under the Constitution, Tax Code and special laws.
   b. Implied exemption or exemption by omission – tax is levied on certain classes without mentioning the other classes. Those not mentioned are deemed tax-exempt.
2. As to Scope or Extent
   a. Total – exempted, expressly or impliedly, from all taxes like non-stock, non-profit educational institutions.
   b. Partial – exempted from certain taxes like minimum wage earners.
3. As to Object
   a. Personal – those granted directly in favor of such persons
   b. Impersonal – those granted directly in favor of a certain class of property.

FORMS OF ESCAPE FROM TAXATION

Exemptions under the Constitution

- From Real Property Tax – real properties actually, directly and exclusively used for religious, charitable or educational purposes.
- From Taxes and Duties – revenues and assets of non-stock, non-profit educational institutions actually, direct

and exclusive used for educational purposes

FORMS OF ESCAPE FROM TAXATION

Exemption under the Tax Code

From Income Tax – income derived from tax-exempt activity by non-stock corporations or associations organized and operated exclusively for religious, charitable, scientific, athletic or cultural purposes.

(BUT, income from property or from any activity conducted for profit, regardless of disposition, is subject to income tax)

From Income Tax – minimum wage, overtime pay, holiday pay, night-shift differential and hazard pay received by a minimum wage earner.

From VAT – monthly rent of residential unit not exceeding P15,000.

From VAT – sale or importation of agricultural and marine food products in the original state.

FORMS OF ESCAPE FROM TAXATION

Exemption under Special Laws

From Income Tax – income from operations of Barangay Micro Business Enterprise (BMBE) (RA No. 9178), but subject to other taxes.

- BMBE – business enterprise engaged in the production, processing or manufacturing of products, including agro-processing, as well as trading and services, with total assets of not more than P3 million.
- Such assets shall include those arising from loans but not the land on which the plant and equipment are located.
- The term "services" shall exclude those rendered by any one, who is duly licensed by the government after having passed a government licensure examination.

From Income Tax – benefit payments to members by GSIS (PD No. 1146) and SSS (RA No. 1161, as amended)

FORMS OF ESCAPE FROM TAXATION

Tax Amnesty

- It is a general pardon or intentional overlooking by the State of its authority to impose penalties on persons otherwise guilty of tax evasion or violation of revenue or tax law.
- It partakes 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.

E.g. Estate Tax Amnesty (RA No. 11213) until June 14, 2021 – net estate of the deceased who died prior to January 1, 2018 subject to 6% amnesty rate without surcharge, interest and penalty.

If will not avail of the amnesty, the net estate is subject to 0%-20% estate tax, plus surcharge, interest and penalty

FORMS OF ESCAPE FROM TAXATION

Differences between Tax Exemption and Tax Amnesty

- In tax amnesty, the taxpayer is immuned from civil, criminal and administrative liabilities, while in tax exemption, the taxpayer is immuned from civil liability only.
- Tax amnesty applies to prior tax periods or retroactively, while tax exemption applies prospectively.

TAX LAWS
NATURE

I. Not Political in Nature – deemed to be the laws of the occupied territory and not of the occupying enemy. E.g. Philippine tax laws continued in force during the period of Japanese occupation and were actually enforced by the occupation government.

II. Civil in Nature – not penal, although penalties are provided for their violation. The purpose in imposing penalties for delinquencies is to compel the timely payment of taxes or to punish evasion or neglect of duty.

TAX LAWS CONSTRUCTION

I. Legislative Intention Must be Considered

- Tax laws are to received a reasonable construction or interpretation with a view to carrying out their purpose and intent. \
- Should not be construed as to permit the taxpayer easily to evade the payment of tax. Thus, good faith is not a valid defense to justify non-payment of tax or surcharge.

II. Where there is No Doubt

- Where the language of the tax stature is plain and there is no doubt as to the legislative intent, the words are to be given their ordinary meaning.

TAX LAWS CONSTRUCTION

III. Where there is Doubt

- Tax statutes are construed strictly against the government and liberally in favor of the taxpayer as taxes are not to be presumed beyond what the statute expressly and clearly declares.
- In case of tax exemptions and refunds, they are construed strictly against the person claiming exemption or refund and liberally in favor of the government. The reason is that taxation is the rule, and exemption is the exception.
  - Exceptions:
  1. When the law itself expressly provides for a liberal construction – In case of doubt, it shall be resolved in favor of exemption.
  2. When the exemption is in favor of the government itself, or its agencies, or of religious, charitable and education institutions.

IV. Where There is Conflict with Other Laws

- National Internal Revenue Code, being a special law, it prevails over a general law like the Civil Code of the Philippines.

TAX LAWS APPLICATION

General Rule: Prospective in operation

Exception: Retroactive provided it is expressly declared or is clearly the legislative intent.

Exception to the Exception: Not to be given retroactive application when it would be harsh and oppressive, for in such case, the constitutional limitation of due process would be violated.

TAX LAWS APPLICATION

Mandatory Provisions – intended for the security of the citizens (like those requiring previous notice to taxpayer of public sale of his property for tax delinquency) or which are designed to insure equality of taxation or certainty as to the nature and amount of each person's tax (Like those prescribing tax rates).

Directory Provisions – designed merely for the information or direction of officers or to secure methodical and systematic modes of proceedings.

Distinction: Omission to follow Mandatory Provisions renders invalid the act or proceeding to which it relates while the omission to follow Directory Provisions does not involve such consequence.

TAX LAWS SOURCES

1. Constitution – ratified by the people.
2. Tax Codes (National Internal Revenue Code, Tariff and Customs Code and portions of the Local Government Code) – enacted by Congress
3. Statutes like RA 1125 as amended (An Act Creating the Court of Tax Appeals), RA 8794 (Law imposing Motor Vehicle User's Charge), PD No. 118, as amended (Law imposing Travel Tax) – enacted by Congress
4. Presidential decrees – issued by the President during martial law.
5. Executive orders – issued by the President under the Provisional Government and pursuant to the legislative power possessed by the President before the convening of Congress on July 27, 1987.
6. Court decision (forms part of the legal system of the Philippines)
7. Revenue regulation promulgated by the Dept. of Finance

TAX LAWS SOURCES

8. Administrative issuances of the BIR Like Revenue Memorandum Circulars and those of the Bureau of Customs like Customs Memorandum Orders
9. BIR rulings
10. Local tax ordinances – enacted by local legislative bodies.
11. Tax treaties and conventions with foreign countries – entered into for the avoidance of international double taxation. Thave the same force and effect as statutes.

TAX LAWS
SOURCES

Revenue Regulations – issuances signed by the Secretary of Finance, upon recommendation of the Commissioner of Internal Revenue, that specify, prescribe or define rules and regulations for the effective enforcement of the National Internal Revenue Code and related statutes.

Nature of Power to Make Regulations under Section 244 of the Tax Code

- Legitimately exercised only for the purpose of implementing the law or putting it into effect.
- The statute which is being administered may not be altered or added to by the exercise of a power to make regulations.
- Regulations cannot increase or decrease the requirements of the law, nor embrace matter not covered or intended to be covered by the statute, otherwise, they are INVALID for being in conflict with the law.

TAX LAWS
SOURCES

Validity of Regulations

Requisites:

- Necessary to the proper enforcement of the law
- Must not be contract to law and the Constitution.
- Must be published in the Official Gazette (the Official Publication of the Government) or a newspaper of general circulation
- Copies thereof must be filed with the University of the Philippine Law Center (Office of the National Administrative Register – the official repository of all the implementing rules and regulations)

Effectivity

- 15 days from the date of filling with the UP Law Center unless a different date is fixed by law, or specified in the rule in cases of imminent danger to public health, safety and welfare.

TAX LAWS
SOURCES

Force and Effect of Regulations

- Have the force and effect of the law
- Binding as if the regulations had been written in the law itself.
- In case of conflict with the law or the Constitution, administrative rules and regulations are null and void.

TAX LAWS
SOURCES

Administrative Interpretations and Opinions

- The power to interpret the provisions of the Tax Code and other tax laws is under the exclusive original jurisdiction of the Commissioner of Internal Revenue subject to review by the Secretary of Finance. (Sec. 4, Tax Code)

- Regulations – formal interpretation of the provision of the Tax Code and other laws by the Secretary of Finance upon recommendation of the Commissioner of Internal Revenue.
- Circular or Memorandum – issuances that publish pertinent and applicable portions, as well as amplifications of laws, rules, regulations and precedents issued by the BIR and other agencies/offices.

TAX LAWS
SOURCES

- Rulings – less general interpretations of tax laws at the administrative level issued by tax officials in the performance of their assessment functions.
  - BIR Rulings – official position of the BIR to queries raised by the taxpayers and other stakeholders relative to clarification and interpretation of tax laws.

❖ Opinions of Secretary of Justice – rulings in the form of opinions on tax questions given by the Secretary of Justice who is the chief legal officer of the government.

Weight Given to Administrative Interpretation

- Entitled to great respect by court.
- But, NOT conclusive and binding upon the courts and will be ignored if judicially found to be erroneous.

TAX LAWS SOURCES

Power of Secretary of Finance to Revoke Rulings of Predecessor

- Rulings of predecessors are not binding upon the Secretary of Finance and if thereafter the Secretary becomes satisfied that a different construction should be given.

Non-retroactivity of Repeal of Regulations or Rulings

General Rule: Not given retroactive application when such revocation, modification or reversal will be prejudicial to the taxpayer. (PROSPECTIVE)

Exceptions (RETROACTIVE):

1. When taxpayer deliberately misstates or omits material facts from his return or in any document required of him by the BIR
2. Where the facts subsequently gathered by the BIR are materially different from facts on which the ruling is based.
3. Where the taxpayer acted in bad faith

TAX LAWS
SOURCES

Decisions of Supreme Court and Court of Tax Appeals

- Binding on all subordinate courts and have the force and effect of a law pursuant to Article 8, Civil Code of the Philippines, which reads:
- "Judicial decisions applying or interpreting the laws or the Constitution shall form a part of the legal system of the Philippines."
- Decisions of Court of Tax Appeals are appealable to the Supreme Court.

THE END