Tax Rulings, Rules, and Regulations in Limbo

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I. INTRODUCTION

The Bureau of Internal Revenue (BIR) is the administrative agency tasked to assess and collect taxes in the Philippines as well as enforce all forfeitures, penalties, and fines connected therewith.[1] The current administration of the

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BIR, headed by the Commissioner of Internal Revenue (CIR) Kim Jacinto-Henares, has been consistently persistent in not only generating more tax revenue for the government,[2] but also in filing tax evasion cases against both corporate and individual taxpayers.[3] This goal is actually in line with the primary purpose of taxation which is to "raise revenue for the support of the government."[4]

One of the programs implemented by the BIR in 2005 is the Run After Tax Evaders (RATE) program,[5] wherein the BIR is mandated to investigate criminal violations of Republic Act (R.A.) No. 8424, otherwise known as the National Internal Revenue Code,[6] "and assist in the prosecution of criminal cases that will generate the maximum deterrent effect, enhance voluntary compliance among taxpayers, and promote public confidence in the tax system."[7] With the goal of generating more tax revenue in mind, the BIR has intensified its efforts to prosecute alleged tax evaders in the country

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601 (2009); and *An Overview of the International Legal Concept of Peace Agreements as Applied to Current Philippine Peace Process*, 53 ATENEO L.J. 263 (2008), with Dean Sedfrey M. Candelaria, Ateneo de Manila University School of Law.

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1. An Act Amending the National Internal Revenue Code, as Amended and for Other Purposes [TAX REFORM ACT OF 1997], Republic Act No. 8424, as Amended, § 2 (1997).
2. *See, e.g.*, Iris C. Gonzales, *BIR exceeds February collection goal*, PHIL. STAR, Mar. 30, 2012, *available at* http://www.philstar.com/Article.aspx?articleId=792370&publicationSubCategoryId=66 (last accessed May 28, 2012).
3. *See, e.g.*, Kristine L. Alave, *BIR vows to continue drive vs tax cheats*, PHIL. DAILY INQ., Sep. 27, 2012, *available at* http://newsinfo.inquirer.net/60159/bir-vows-to-continue-drive-vs-tax-cheats (last accessed May 28, 2012).
4. HECTOR S. DE LEON & HECTOR M. DE LEON, JR., THE FUNDAMENTALS OF TAXATION 9 (14th ed. 2004) [hereinafter DE LEON & DE LEON, JR., TAXATION].
5. Bureau of Internal Revenue, Re-invigorating the Run After Tax Evaders (RATE) Program and Amending Certain Portions of RMO No. 24-2008, Revenue Memorandum Order No. 27-2010 [BIR RMO No. 27-2010] (Mar. 15, 2010). *See also* Bureau of Internal Revenue, Policies and Guidelines for RATE Cases, Revenue Memorandum Order No. 24-2008 [BIR RMO No. 24-2008] (May 9, 2008).
6. *See generally* TAX REFORM ACT OF 1997, tit. IC.
7. Bureau of Internal Revenue, Run Against Tax Evaders (RATE) Program, *available at* ftp://ftp.bir.gov.ph/webadmin1/pdf/rate_background_and_organization.pdf (last accessed May 28, 2012).

under the RATE program,[8] and has issued rulings and regulations, some of which have significantly changed the positions of the BIR on tax matters which have been consistently upheld in the past years and which may have no basis under Philippine and international law.

II. RULE-MAKING POWER OF THE BIR

A. Rule-Making Power in General

One of the powers endowed to administrative agencies, such as the BIR, is the quasi-legislative or rule-making power.[9] Rule-making is "the power to make implementing or interpretative rules or regulations ... [which] results in 'delegated legislation.'"[10] It is "legislation within the confines of the granting statute, as required by the Constitution and its doctrine of non-delegability and separability of certain powers flowing from the separation of the three branches of the government."[11]

B. Limitations on the Rule-Making Power

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8. *See* Bureau of Internal Revenue, BIR ties up with NBI and CIDG for prosecution of tax evaders, *available at* ftp://ftp.bir.gov.ph/webadmin1/pdf/reinvigorated_rate.pdf (last accessed May 28, 2012).

9. HECTOR S. DE LEON & HECTOR M. DE LEON, JR., ADMINISTRATIVE LAW: TEXT AND CASES 78 (6th ed. 2010) [hereinafter DE LEON & DE LEON, JR., ADMINISTRATIVE LAW].

10. *Id.* at 80.

11. *Id.* (citing 1 AM. JUR. 2D 891). De Leon and De Leon, Jr. explain the doctrine of separation of powers, thus —

> The doctrine declares that governmental powers are divided among the three departments of government, the legislative, executive, and judicial, and broadly operates to confine legislative powers to the legislature, executive powers to the executive department, and judicial powers to the judiciary, precluding one branch of the government from exercising or invading the powers of another.

DE LEON & DE LEON, JR., ADMINISTRATIVE LAW, at 170 (citing Angara v. Electrical Commission, 63 Phil. 139 (1936) & People v. Vera, 65 Phil. 56 (1937)).

De Leon and De Leon, Jr. go on to state that the doctrine of non-delegation of powers, which

> follows as a necessary corollary of the doctrine of separation of powers[,] prohibits the delegation of legislative power, the vesting of judicial officers with non-judicial functions, as well as the investing of non-judicial officers with judicial powers. Any attempt at such delegation is unconstitutional and void.

DE LEON & DE LEON, JR., ADMINISTRATIVE LAW, at 171 (citing *Vera*, 65 Phil. at 56).

The BIR, as a public administrative body, "may make only such rules and regulations as are within the limits and powers granted to it."[12] This means that the BIR "may not make rules and regulations which are inconsistent with the provisions of the Constitution or of a statute, particularly the [National Internal Revenue Code], or which are in derogation of, or defeat, the purpose of such statute."[13] Further, the BIR cannot "by its rules and regulations, amend, alter, modify, supplant, enlarge or expand, restrict or limit the provisions or coverage of the statute,"[14] nor can it make a rule or regulation which is unreasonable and unfair or discriminatory.[15] Rules and regulations which have the "effect of extending, or which conflict with the authority-granting statute do not represent a valid exercise of the rule-making power but constitute an attempt by an administrative body to legislate."[16]

C. Requisites for Validity of Administrative Rules and Regulations

Valid administrative rules and regulations — those which are in consonance with the general purposes and objects of the law — have the same binding force and effect as valid statutes.[17] The requisites for validity of administrative rules and regulations are as follows:

(1) The rules and regulations must have been issued under the authority of law;

(2) They must not be contrary to law and the Constitution; and

(3) They must be promulgated in accordance with the prescribed procedure.[18]

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12. DE LEON & DE LEON, JR., ADMINSTRATIVE LAW, *supra* note 9, at 81.

13. *Id.* (citing Phil. International Trading Corp. v. Commission on Audit, 416 SCRA 245 (2003) & Conte v. Commission on Audit, 264 SCRA 19 (1996)).

14. DE LEON & DE LEON, JR., ADMINISTRATIVE LAW, *supra* note 9, at 81 (citing 73 C.J.S. 413-14 & 416-17; Toledo v. Civil Service Commission, 202 SCRA 507 (1991); Luzon Polymers Corporation v. Clave, 209 SCRA 711 (1992); Comm. of Internal Revenue v. Court of Appeals, 240 SCRA 368 (1995); Republic v. Court of Appeals, 324 SCRA 237 (2000); Comm. of Internal Revenue v. Central Luzon Drug Corporation, 456 SCRA 414 (2005); & MCC Industrial Sales Corp. v. Ssangyong Corp., 536 SCRA 408 (2007)).

15. DE LEON & DE LEON, JR., ADMINISTRATIVE LAW, *supra* note 9, at 82.

16. *Id.* (citing People v. Maceren, 79 SCRA 450 (1977) & United BF Homeowner's Association v. BF Homes, Inc., 310 SCRA 304 (1999)).

17. DE LEON & DE LEON, JR., ADMINISTRATIVE LAW, *supra* note 9, at 88. *See also* De Guzman v. Lontok, 68 Phil. 405, 411-12 (1939).

18. DE LEON & DE LEON, JR., ADMINISTRATIVE LAW, *supra* note 9, at 97 (citing Pagpalain Haulers, Inc. v. Trajano, 310 SCRA 354 (1999) & Department of Agrarian Reform v. Sutton, 473 SCRA 391 (2005)).

Furthermore, they must be reasonable and published in the Official Gazette or in a newspaper of general circulation.[19]

Rules and regulations "enacted by the administrative authorities pursuant to the powers delegated to them have the force and effect of law,"[20] hence, are entitled to great respect.[21] They also have in their favor the presumption of legality unless they appear to be clearly unreasonable or arbitrary.[22]

D. Rule-Making Power of the BIR

Section 244 of the National Internal Revenue Code provides —

> SEC. 244. Authority of Secretary of Finance to Promulgate Rules and Regulations. — The Secretary of Finance, upon recommendation of the Commissioner, shall promulgate all needful rules and regulations for the effective enforcement of the provisions of this Code.[23]

The administrative power of the Secretary of Finance to provide regulations is likewise authorized by Book IV, Section 7[24] and Book IV, Title II, Section 18[25] of the Administrative Code of 1987.

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19. ANTONIO B. NACHURA, OUTLINE/REVIEWER IN POLITICAL LAW 395 (2006).
20. Carolina Industries, Inc. v. CMS Stock Brokerage Inc., 97 SCRA 734, 760 (1980) (citing Geukeko v. Araneta, etc., 102 Phil. 706, 713 (1957)).
21. Gonzales v. Land Bank of the Philippines, 183 SCRA 520, 526 (1990).
22. *Id.* (citing Español v. Chairman, PVA, 137 SCRA 315 (1986)).
23. TAX REFORM ACT OF 1997, § 244.
24. Instituting the "Administrative Code of 1987" [ADMINISTRATIVE CODE OF 1987], Executive Order No. 292, as Amended, bk. IV, § 7 (1987). This Section provides —

    > Section 7. *Powers and Functions of the Secretary*. — The Secretary shall:
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    > ...
    >
    > (3) Promulgate rules and regulations necessary to carry out department objectives, policies, functions, plans, programs and projects.

    Id.
25. *Id.* bk. IV, tit. II, § 18. This Section provides —

    > Section 18. *The Bureau of Internal Revenue*. — The Bureau of Internal Revenue, which shall be headed by and subject to the supervision and control of the Commissioner of Internal Revenue who shall be appointed by the President upon the recommendation of the Secretary shall have the following functions:
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    > ...
    >
    > The Commissioner of Internal Revenue, with the approval of the Secretary of Finance, shall draft and prepare the necessary rules and

The more specific interpretations of tax laws at the administrative level are called BIR rulings.[26] Such rulings are "issued by tax officials in the performance of their assessment functions."[27] They are usually rendered by the CIR upon the request of taxpayers to confirm or clarify certain provisions of a tax law,[28] in the exercise of the power provided for under Section 4 of the National Internal Revenue Code, to wit —

> SEC. 4. Power of the Commissioner to Interpret Tax Laws and to Decide Cases. — The power to interpret the provisions of this Code and other tax laws shall be under the exclusive and original jurisdiction of the Commissioner, subject to review by the Secretary of Finance.
>
> The power to decide disputed assessments, refunds of internal revenue taxes, fees or other charges, penalties imposed in relation thereto, or other matters arising under this Code or other laws or portions thereof administered by the Bureau of Internal Revenue is vested in the Commissioner, subject to the exclusive appellate jurisdiction of the Court of Tax Appeals.[29]

On 26 May 2007, by virtue of Revenue Memorandum Circular (RMC) No. 37-2007,[30] the CIR delegated the authority to sign rulings granting and/or confirming tax exemptions, tax incentives, as well as tax treaty relief through the ruling process to the Deputy Commissioner for Legal & Inspection Group and to the Assistant Commissioner for Legal Service.[31]

The aforementioned BIR rulings "may be revoked by the Secretary of Finance if the latter finds them not in accordance with law."[32]

III. DEVELOPMENTS ON TAX MATTERS

A. Mandatory Filing of a Tax Treaty Relief Application (TTRA) Before a Preferential Tax Treaty Rate Can Be Applied

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> regulation as may be needed to delineate the authority and responsibility of the various groups and services of the Bureau.

Id.

26. DE LEON & DE LEON, JR., TAXATION, *supra* note 4, at 80.

27. *Id.*

28. *Id.*

29. TAX REFORM ACT OF 1997, § 4.

30. Bureau of Internal Revenue, Delegation of Authority to Sign Rulings Granting and/or Confirming Tax Exemptions, Tax Incentives as well as Tax Treaty Relief Through the Ruling Process, Revenue Memorandum Circular No. 37-2007 [BIR RMC No. 37-2007] (May 26, 2007).

31. *Id.* §§ 1-2.

32. DE LEON & DE LEON, JR., TAXATION, *supra* note 4, at 80.

The BIR has taken the stand that a TTRA must first be filed before availing of the preferential tax rates provided for in tax treaties entered into by the Philippines with other countries.[33]

The BIR supports its stand by issuing and strictly implementing Revenue Memorandum Order (RMO) No. 72-2010[34] dated 25 August 2010, which prescribes the documentary requirements for the processing of a TTRA. The general documentary requirements enumerated in RMO No. 72-2010, which should be attached to the duly accomplished application of the applicant,[35] who may be the income earner or his duly authorized representative,[36] are as follows: (1) Proof of Residency;[37] (2) Articles of Incorporation;[38] (3) Special Power of Attorney;[39] (4) Certificate of Business Presence or No Business Presence in the Philippines issued by the Philippine Securities and Exchange Commission for a corporation or partnership or by the Department of Trade and Industry for an individual;[40] and (5) Certificate of No Pending Case.[41] These documents, in addition to the other documents required, depending on the purpose for which the TTRA is filed, are required to be authenticated or consularized by the Philippine embassy if executed abroad.[42]

Other than the documentary requirements to be filed together with the application, RMO No. 72-2010 requires that the application be filed with

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33. Rester John Lao Nonato, *Void tax treaty requirements*, CEBU DAILY NEWS, Apr. 27, 2012, *available at* http://newsinfo.inquirer.net/183455/void-tax-treaty-requirements (last accessed May 28, 2012) [hereinafter Nonato, *Void tax treaty requirements 1*].

34. Bureau of Internal Revenue, Guidelines on the Processing of Tax Treaty Relief Applications (TTRA) Pursuant to Existing Philippine Tax Treaties, Revenue Memorandum Order No. 72-2010 [BIR RMO No. 72-2010] (Aug. 25, 2010).

35. *Id.* § 3.

36. *Id.*

37. *Id.* § 3 (1).

38. *Id.* § 3 (2).

39. *Id.* § 3 (3).

40. BIR RMO No. 72-2010, § 3 (4).

41. *Id.* § 3 (5).

42. *Id.* § 3. *See also* BIR RMO No. 72-2010, § 13 (2). Section 13 defines consularized to mean

> that the document should be accompanied a certificate issued by a secretary of the embassy or legation, consul general, consul, vice consul, or consular agent or by any officer in the foreign service of the Philippines stationed in the country where such document was executed.

Id. § 13 (2).

the International Tax Affairs Division (ITAD) of the BIR *before the transaction*,[43] which is defined in the same RMO as follows:

> *First taxable event for purposes of filing the [TTRA], shall mean the first or the only time when the income payor is required to withhold the income tax thereon or should have withheld taxes thereon had the transaction been subjected to tax*; and for 0901-C applications, before the due date of the Documentary Stamp Tax (DST) on the sale of the shares of stock.[44]

Since the issuance of RMO No. 72-2010, the BIR has consistently issued rulings granting the tax treaty relief sought for by the applicant as long as the application, together with the complete set of supporting documents, is filed before the first taxable event.[45] However, the position of the BIR recently changed as it started to issue rulings denying the tax treaty relief sought for by the applicant[46] due to the reasoning that the TTRA was filed beyond the 15-day period prescribed in RMO No. 01-2000,[47] dated 25 November 1999, the RMO issued prior to RMO No. 72-2010.

Section III (2) of RMO No. 1-2000 provides —

> III. Policies:
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> In order to achieve the above-mentioned objectives, the following policies shall be observed:
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> ...
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> (2) *Any availment of the tax treaty relief shall be preceded by an application* by filing BIR Form No. 0901 (Application for Relief from Double Taxation) with ITAD *at least 15 days before the transaction* i.e.[,] payment

43. *Id.* § 14.

44. *Id.* § 13 (4) (emphasis supplied).

45. *See* Bureau of Internal Revenue, Ruling No. ITAD 203-11 [BIR Ruling No. ITAD 203-11] (July 27, 2011) & Bureau of Internal Revenue, Ruling No. ITAD 189-11 [BIR Ruling No. ITAD 189-11] (July 7, 2011).

46. *See* Bureau of Internal Revenue, Ruling No. ITAD 098-12 [BIR Ruling No. ITAD 098-12] (Feb. 17, 2012); Bureau of Internal Revenue, Ruling No. ITAD 096-12 [BIR Ruling No. ITAD 096-12] (Feb. 16, 2012); Bureau of Internal Revenue, Ruling No. ITAD 297-11 [BIR Ruling No. ITAD 297-11] (Nov. 25, 2011); Bureau of Internal Revenue, Ruling No. ITAD 296-11 [BIR Ruling No. ITAD 296-11] (Nov. 25, 2011); Bureau of Internal Revenue, Ruling No. ITAD 295-11 [BIR Ruling No. ITAD 295-11] (Nov. 25, 2011); & Bureau of Internal Revenue, Ruling No. ITAD 285-11 [BIR Ruling No. ITAD 285-11] (Nov. 18, 2011).

47. Bureau of Internal Revenue, Procedures for Tax Treaty Relief Application, Revenue Memorandum Order No. 1-2000 [BIR RMO No. 1-2000], III (2) (Nov. 25, 1999).

> of dividends, royalties, etc., accompanied by supporting documents justifying the relief.[48]

One of the recent applications denied by the BIR applying the aforementioned provision and reasoning is BIR Ruling No. ITAD 147-12,[49] dated 2 April 2012. In this case, Kirin Holdings Company Limited filed a TTRA on 7 August 2009 requesting for confirmation that the 15% preferential tax rate be applicable on the dividends received by them from San Miguel Corporation pursuant to the Philippines-Japan Tax Treaty.[50] The dividends received by Kirin Holdings Company Limited were paid on 10 August 2009.[51] The pertinent portion of the ruling is quoted as follows —

> In view of the foregoing, *since the dividends received by Kirin Holdings Company Limited were paid on [10 August 2009] and the subject TTRA was only filed on [7 August 2009] in violation of Section III (2) of RMO 1-2000, this Office hereby DENIES the TTRA for having been filed beyond the 15-day period prescribed by the RMO.* Accordingly, the subject dividends shall be subject to income tax at the rate of 30% as provided under Section 28 (B) (1) of the 1997 National Internal Revenue Code, as amended.[52]

The ruling cited *Mirant (Philippines) Operations Corporation v. Commissioner of Internal Revenue*,[53] dated 7 June 2005, as one of its bases to deny the TTRA of Kirin Holdings Company Limited. *Mirant (Philippines) Operations Corporation* provides —

> *However, it must be remembered that a foreign corporation wishing to avail of the benefits of the tax treaty should invoke the provisions of the tax treaty and prove that indeed the provisions of the tax treaty* applies to it, before the benefits may be extended to such corporation. In other words, a resident or non-resident foreign corporation shall be taxed according to the provisions of the National Internal Revenue Code, unless it is shown that the treaty provisions apply to the said corporation, and that, in cases the same are applicable, the option to avail of the tax benefits under the tax treaty has been successfully invoked.
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> *Under Revenue Memorandum Order 01-2000 of the Bureau of Internal Revenue, it is provided that the availment of a tax treaty provision must be preceded by an application for a tax treaty relief with its [ITAD].* This is to prevent any erroneous interpretation and/or application of the treaty provisions with

48. *Id.* (emphasis supplied).

49. Bureau of Internal Revenue, Ruling No. ITAD 147-12 [BIR Ruling No. ITAD 147-12] (Apr. 2, 2012).

50. *Id.*

51. *Id.*

52. *Id.* (emphasis supplied).

53. Mirant (Philippines) Operations Corporation v. Commissioner of Internal Revenue, CTA-E.B. No. 40, (June 7, 2005).

> which the Philippines is a signatory to. The implementation of the said Revenue Memorandum Order is in harmony with the objectives of the contracting state to ensure that the granting of the benefits under the tax treaties are enjoyed by the persons or corporations duly entitled to the same.[54]

In the aforementioned ruling, the CIR used RMO No. 01-2000 as her basis. It is important to note that RMO No. 72-2010, the latest RMO setting forth the guidelines for tax treaty applications, provides that the application should be filed before the first taxable event.[55] Nowhere in RMO No. 72-2010 did it mention that that the application should be filed at least 15 days before the transaction or first taxable event or else the application would be denied.[56]

Moreover, Section 20 of RMO No. 72-2010 provides —

> SECTION 20. REPEALING CLAUSE. — *Any revenue issuance which is inconsistent with this Order is deemed* revoked, repealed, or *modified accordingly*.[57]

Hence, the provisions of RMO No. 72-2010 should prevail as to when the TTRA should be filed, and not that of RMO No. 01-2000. Even if it can be argued that the TTRA of Kirin Holdings Company Limited was filed on 7 August 2009, which was before RMO No. 72-2010 was issued and became effective, it can be argued that amendatory rulings and regulations may be applied retroactively if such is beneficial or favorable to the party or the taxpayer.[58] This is more in keeping with the spirit of fairness and equity. Conversely, it is important to note that the National Internal Revenue Code provides that rules and regulations as well as rulings or circulars promulgated by the CIR which are prejudicial to taxpayers are not given retroactive application.[59]

Contrary to BIR Ruling No. ITAD 147-12, the BIR approved the confirmatory ruling sought for by the taxpayer in DA ITAD BIR Ruling

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54. *Id.* (emphasis supplied).

55. BIR RMO No. 72-2010, § 14.

56. *See generally* BIR RMO No. 72-2010.

57. *Id.* § 20 (emphasis supplied).

58. Fort Bonifacio Development Corporation v. Commissioner of Internal Revenue, 583 SCRA 168, 206 (2009) (J. Ynares-Santiago, concurring opinion). In her concurring opinion, Justice Ynares-Santiago concluded that —

> While the events subject of G.R. No. 158885 took place before the issuance of Rev. Regs. 6-97, this regulation must be given retroactive application, it being beneficial to the taxpayer.

Id.

59. TAX REFORM ACT OF 1997, § 246.

No. 112-09,[60] dated 28 December 2009. In the latter case, TI (Philippines) Inc. (TIPI) filed a TTRA with the BIR on 21 December 2009, requesting for confirmation that dividends to be received by Texas Instruments Holland B.V. (TI-Holland) from TIPI are subject to a preferential tax rate of 10% pursuant to the Philippines-Netherlands tax treaty.[61] On 21 December 2009, "the Board of Directors of TIPI declared a cash dividend in the amount of [$10,000,000.00], payable to all stockholders of TIPI as of the date of the meeting, as soon as practicable but in any event no later than 31 December 2009."[62] The CIR here held that "the dividend payments by TIPI pertaining to TI-Holland shall be subject to a preferential tax rate of 10[%], based on the gross amount of dividends, pursuant to Article 10 (2) (a) of the Philippines-Netherlands tax treaty."[63]

It should be noted that in DA ITAD BIR Ruling No. 112-09, the TTRA was filed before the dividends were paid by TIPI but failed to comply with the 15-day period requirement.[64] The same facts occurred in BIR Ruling No. ITAD 147-12, where the TTRA was filed by Kirin Holdings Company Limited three days before the dividends were paid.[65] In the former ruling, the preferential tax treaty rate was approved while in the latter, it was denied. The Author is at a loss as to why the recent TTRAs have been denied by the CIR based on the reasoning that the TTRA failed to comply with the 15-day requirement when in fact such TTRA was filed before the first taxable event as required by RMO No. 72-2010.

Furthermore, the requirement of a TTRA itself before any tax relief can be availed of by the applicant taxpayer has already no legal basis by itself, for tax treaty obligations should not be restricted by mere regulations or revenue memorandum orders such as RMO Nos. 01-2000 and 72-2010.

A treaty is defined as an "international agreement concluded between States in written form and governed by international law, whether embodied in a single instrument or in two or more instruments and whatever its particular designation."[66] As defined, treaties, including tax treaties, should be governed by international law.

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60. Bureau of Internal Revenue, DA ITAD BIR Ruling No. 112-90 [DA ITAD BIR Ruling No. 112-90] (Dec. 28, 2009).

61. *Id.*

62. *Id.*

63. *Id.*

64. *Id.*

65. BIR Ruling No. ITAD 147-12.

66. NACHURA, *supra* note 19, at 660 (citing Vienna Convention on the Law of Treaties art. II (1) (a), *adopted* May 23, 1969, 1155 U.N.T.S. 331 (entered into force Jan. 27, 1980)).

The fundamental principle of "*pacta sunt servanda* [ ] requires that treaties must be observed in good faith."[67] In *La Chemise Lacoste, S.A. v. Fernandez*,[68] dated 21 May 1984, the Supreme Court ruled as follows —

> The memorandum is a clear manifestation of our avowed adherence to a policy of cooperation and amity with all nations. It is not, as wrongly alleged by the private respondent, a personal policy of Minister Luis Villafuerte which expires once he leaves the Ministry of trade. *For a treaty or convention is not a mere moral obligation to be enforced or not at the whims of an incumbent head of a Ministry. It creates a legally binding obligation on the parties founded on the generally accepted principle of international law of pacta sunt servanda which has been adopted as part of the law of our lana.* ... The memorandum reminds the Director of Patents of his legal duty to obey both law and treaty. It must also be obeyed.[69]

In the Philippines, it has already been established that there is no substantial distinction between international law and municipal law.[70] Hence, treaties and national laws are treated equally. What the Philippines adopts is "the Monistic Theory in International Law in the interpretation of statutes and treaties. Because of this rule, treaties and statutes are generally interpreted to complement one another."[71]

Moreover, Section 2 of Article II of the 1987 Constitution provides that the Philippines "adopts the generally accepted principles of international law as part of the law of the land."[72] Indeed, "[i]nternational law does not need to be translated into national law. The act of ratifying the international law immediately incorporates the law into national law."[73]

Prior to the issuance of RMO Nos. 01-2000 and 72-2010, the provisions of the tax treaties entered into by the Philippines with other countries were applied without the need of filing a TTRA with the BIR. In *Commissioner of Internal Revenue v. Procter & Gamble Philippine Manufacturing Corporation*,[74] the Supreme Court acknowledged that the Philippines-United States tax treaty established a treaty commitment on the part of both parties to reduce the regular rate of dividend tax to a maximum rate of 20%, to wit —

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67. NACHURA, *supra* note 19, at 664.

68. La Chemise Lacoste, S.A. v. Fernandez, 129 SCRA 373 (1984).

69. *Id.* at 390 (citing PHIL. CONST. art. II, § 2) (emphasis supplied).

70. Rester John Lao Nonato, *Void tax treaty requirements*, CEBU DAILY NEWS, Apr. 30, 2012, at 27 [hereinafter, Nonato, *Void tax treaty requirements 2*].

71. *Id.*

72. PHIL. CONST. art. II, § 2.

73. Nonato, *Void tax treaty requirements 2*, *supra* note 70, at 29.

74. Commissioner of Internal Revenue v. Procter & Gamble Philippine Manufacturing Corporation, 204 SCRA 377 (1991).

> It remains only to note that under the Philippines-United States Convention 'With Respect to Taxes on Income,' the Philippines, *by a treaty commitment*, reduced the regular rate of dividend tax to a maximum of [20%] of the gross amount of dividends paid to US parent corporations:
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> ...
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> The Tax Convention, at the same time, established a treaty obligation on the part of the United States that it 'shall allow' to a US parent corporation receiving dividends from its Philippine subsidiary 'a [tax] credit for the appropriate amount of taxes paid or accrued to the Philippines by the Philippine [subsidiary] —.' This is, of course, precisely the 'deemed paid' tax credit provided for in Section 902, US Tax Code, discussed above. Clearly, there is here on the part of the Philippines a deliberate undertaking to reduce the regular dividend tax rate of [35%]. Since, however, the treaty rate of [20%] is a *maximum* rate, there is still a differential or additional reduction of five [ ] percentage points which compliance of US law (Section 902) with the requirements of Section 24 (b) (1), NIRC, makes available in respect of dividends from a Philippine subsidiary.
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> We conclude that private respondent P&G-Phil, is entitled to the tax refund or tax credit which it seeks.[75]

Although the Court of Tax Appeals has upheld the position of the BIR in *Deutsche Bank AG Manila Branch v. Commissioner of Internal Revenue*,[76] dated 29 August 2008, that compliance with the procedural requirements provided under RMO Nos. 01-2000 and 72-2010 are mandatory,[77] the Author believes otherwise as explained above. While the Author acknowledges that administrative regulations have the presumption of validity and legality,[78] the Author also believes that such regulations, when they add additional burdens to the fulfillment of the Philippines' treaty commitments and obligations, should be voided for going against the rule of *pacta sunt servanda*.[79]

B. Transfer of Properties as Liquidating Dividends are Subject to Income Tax

The BIR, in past rulings, has held that a liquidating corporation does not realize gain or loss in partial or complete liquidation, hence, it is not liable for income tax and conversely, such corporation is not subject to tax on the

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75. *Id.* at 401-03 (citing Philippine-United States Convention "With Respect to Taxes on Income," Phil.-U.S., art. 23 (1), Oct. 1, 1976, 7 P.T.S. 523 (entered into force Oct. 16, 1982)).

76. Deutsche Bank AG Manila Branch v. Commissioner of Internal Revenue, CTA. Case No. 7344, Aug. 29, 2008.

77. *Id.*

78. Chevron Philippines, Inc. v. Bases Conversion Development Authority, 630 SCRA 519, 530 (2010).

79. Nonato, *Void tax treaty requirements 1*, *supra* note 33.

receipt of shares surrendered by its shareholders pursuant to a complete or partial liquidation.[80] Moreover, the BIR has held that a liquidating gain or loss is in the nature of capital gain or loss from sale or exchange of shares and is subject to the ordinary income tax rates under the National Internal Revenue Code, depending on the status of the shareholder.[81]

The aforementioned ruling is consistent with the decision of the Supreme Court in *Wise & Co. v. Meer*,[82] to wit —

> It should be borne in mind that plaintiffs received the distributions in question in exchange for the surrender and relinquishment by them of their stock in the Hongkong Company which was dissolved and in process of complete liquidation. That money in the hands of the corporation formed a part of its income and was properly taxable to it under the then existing Income Tax Law. *When the corporation was dissolved and in process of complete liquidation and its shareholders surrendered their stock to it and it paid the sums in question to them in exchange, a transaction took place, which was no different in its essence from a sale of the same stock to a third party who paid therefor.*[83]

Revenue Regulation (RR) No. 006-08,[84] dated 22 April 2008, supports the position that liquidating gain is to be treated as the gain from the sale or exchange of shares. Section 8 of such regulation provides —

> SECTION. 8. Taxation of Surrender of Shares by the Investor Upon Dissolution of the Corporation and Liquidation of Assets and Liabilities of Said Corporation. — *Upon surrender by the stockholder of its shares in exchange for cash and property distributed by the issuing corporation upon its dissolution and liquidation of all assets and liabilities, the investor shall recognize either capital gain or loss* upon such surrender of shares computed by comparing the cash and fair market value of property received against the cost of the investment in

80. *See* Bureau of Internal Revenue, Ruling No. 039-02 [BIR Ruling No. 039-02] (Nov. 11, 2002) & Bureau of Internal Revenue, Ruling No. 171-92 [BIR Ruling No. 171-92] (May 28, 1992).

81. *Id. See also* Bureau of Internal Revenue, Ruling No. 190-84 [BIR Ruling No. 190-84] (Dec. 21, 1984); Bureau of Internal Revenue, Ruling No. 322-87 [BIR Ruling No. 322-87] (Oct. 19, 1987); Bureau of Internal Revenue, Ruling No. 136-88 [BIR Ruling No. 136-88] (Apr. 12, 1988); Bureau of Internal Revenue, Ruling No. 021-89, [BIR Ruling No. 021-89] (Feb. 13, 1989); Bureau of Internal Revenue, Ruling No. 270-91 [BIR Ruling No. 270-91] (Dec. 23, 1991); Bureau of Internal Revenue, Ruling No. DA-214-96 [BIR Ruling No. DA-214-96] (June 26, 1996); & Bureau of Internal Revenue, Ruling No. DA-223-98 [BIR Ruling No. DA-223-98] (June 8, 1998).

82. Wise & Co. v. Meer, 78 Phil. 655 (1947).

83. *Id.* at 672-73 (emphasis supplied).

84. Bureau of Internal Revenue, Consolidated Regulations Prescribing the Rules on the Taxation of Sale, Barter, Exchange or Other Disposition of Shares of Stock Held as Capital Assets, Revenue Regulation No. 006-08 [BIR Rev. Reg. No. 006-08] (Apr. 22, 2008).

> shares. The difference between the sum of the cash and the fair market value of property received and the cost of the investment in shares shall represent the capital gain or capital loss from the investment, whichever is applicable.[85]

On 5 December 2011, the BIR changed its position relative to the tax treatment of liquidating dividends when the Office of the CIR issued BIR Ruling No. 479-11.[86] In this case, the corporate term of Aguirre Pawnshop Company, Inc. (APC) expired on 14 December 2006 and accordingly, APC ceased to exist as a corporate entity and was dissolved *ipso facto*.[87] On 1 December 2009, the Board of Directors of APC, in their capacity as Trustees of the corporate assets, ordered "the distribution of the remaining assets of APC to its stockholders by way of liquidating dividends."[88] APC requested for confirmation that it was not liable for income tax either on its transfer of the properties to its stockholders as liquidating dividends or in its receipt of the surrendered shares of its stockholders, citing BIR Ruling No. 039-02 dated 11 November 2002 as one of its basis.[89] The BIR here held —

> In reply, please be informed that it is the position of this Office that *your request cannot be granted for lack of legal basis under the National Internal Revenue Code of 1997*, as amended. Consequently, the previously issued BIR Ruling No. 039-02 cited in your letter and the BIR Rulings cited in the said ruling are reversed and set aside.[90]

No further reasoning and discussion for the denial of the request for confirmation were stated in the ruling. There was also no explanation to guide taxpayers on how to treat the liquidating dividends.[91]

Considering that APC filed its request for confirmatory ruling on 18 August 2010, more than a year before the BIR issued its simple and unqualified denial, "[t]he least that the BIR could have done in the spirit of fairness and consistent with the principles of due process was to educate or inform the requestor the reasons and rationale behind its denial."[92] Even

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85. *Id.* § 8 (emphasis supplied).

86. Bureau of Internal Revenue, Ruling No. 479-11 [BIR Ruling No. 479-11] (Dec. 5, 2011).

87. *Id.*

88. *Id.*

89. *Id.*

90. *Id.* (emphasis supplied).

91. Tata Panlilo-Ong, Tax treatment of liquidating dividends in limbo, *available at* http://www.punongbayan-araullo.com/pnawebsite/pnahome.nsf/section_docs/TS753U_27-3-12 (last accessed May 28, 2012).

92. Rester John Nonato, *Due process rulings*, CEBU DAILY NEWS, Apr. 20, 2012, *available at* http://newsinfo.inquirer.net/179607/due-process-rulings (last accessed May 28, 2012).

more so, given that the main purpose for the issuance of rulings by the BIR was "to clear out any doubts on matters involving our tax laws," rules, and regulations.[93]

By not giving the rationale behind the denial of APC's request for confirmation, the BIR seems to have denied APC of its property right without due process of law[94] as laid out in Section 1, Article III of the Constitution, which provides —

> Section 1. 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 the laws.[95]

C. Tax Credit Certificates (TCCs) are Not Transferable

TCCs are issued to taxpayers to indicate their tax credits in lieu of a cash refund and may be used to pay any of their internal revenue tax liability.[96] This is enunciated in Section 204 (C) of the National Internal Revenue Code, to wit —

> SEC. 204. Authority of the Commissioner to Compromise, Abate and Refund or Credit Taxes. — *The Commissioner may* —
>
> ...
>
> (C) Credit or refund taxes erroneously or illegally received or penalties imposed without authority, refund the value of internal revenue stamps when they are returned in good condition by the purchaser, and, in his discretion, redeem or change unused stamps that have been rendered unfit for use and refund their value upon proof of destruction. No credit or refund of taxes or penalties shall be allowed unless the taxpayer files in writing with the Commissioner a claim for credit or refund within two (2) years after the payment of the tax or penalty: Provided, however, That a return filed showing an overpayment shall be considered as a written claim for credit or refund.
>
> *A Tax Credit Certificate validly issued under the provisions of this Code may be applied against any internal revenue tax, excluding withholding taxes, for which the taxpayer is directly liable.* Any request for conversion into refund of unutilized tax credits may be allowed, subject to the provisions of Section 230 of this Code: *Provided*, That the original copy of the Tax Credit Certificate showing a creditable balance is surrendered to the appropriate revenue officer for verification and cancellation: *Provided, further*, That in no

93. *Id.*

94. *Id.*

95. PHIL. CONST. art. III, § 1.

96. *But see* Iris C. Gonzales, *Gov't abolishes tax credit certificate system*, PHIL. STAR, Apr. 3, 2012, *available at* http://www.philstar.com/Article.aspx?publicationSubCategoryId=66&articleId=793700 (last accessed May 28, 2012).

> case shall a tax refund be given resulting from availment of incentives granted pursuant to special laws for which no actual payment was made.[97]

In accordance with the spirit of fairness, the BIR returns to the taxpayers their excess taxes or erroneously paid taxes either by tax credit or cash refund. The "taxpayer is given the choice whether to claim for refund or have its excess taxes applied as tax credit for the succeeding taxable year,"[98] although such election is not final since prior verification and approval by the CIR is required.[99] In most cases, taxpayers would opt for the issuance of TCCs rather than cash refunds since the latter would require a longer period for approval and would entail availability of funds, which requires prior appropriation by Congress.[100]

Under RR No. 05-2000,[101] dated 15 August 2000, TCCs issued by the BIR may be transferred in favor of an assignee subject to the following conditions:

> (i) The transfer must be with prior approval of the Commissioner or his duly authorized representative who shall verify whether or not the TCC sought to be transferred is still valid in the hands of the original holder;
>
> (ii) The transfer should be limited to one transfer only; and
>
> (iii) The transferee shall use the TCC assigned to him strictly in payment of his direct internal revenue tax liability and in no case shall the same be available for conversion to cash in his hands.[102]

On 29 July 2011, RR No. 14-2011[103] was issued which amended Section 4 of RR No. 5-2000, disallowing all TCCs issued by the BIR to be

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97. TAX REFORM ACT OF 1997, § 204 (C) (emphasis supplied).

98. Paseo Realty & Development Corporation v. Court of Appeals, 440 SCRA 235, 249 (2004).

99. *Id.*

100. Lesley G. Lato, A shift from TCCs to cash refunds, *available at* http://www.punongbayan-araullo.com/pnawebsite/pnahome.nsf/section_docs/KD570D_16-8-11 (last accessed May 28, 2012).

101. Bureau of Internal Revenue, Prescribing the Regulations Governing the Manner of the Issuance of Tax Credit Certificates, and the Conditions for their Use, Revalidation and Transfer, Revenue Regulation No. 05-00 [BIR Rev. Reg. No. 05-00] (July 19, 2000).

102. *Id.* § 4 (a).

103. Bureau of Internal Revenue, Amending Certain Provision of Revenue Regulation No. 5-2000 as amended, Prescribing the Regulations Governing the Manner of the Issuance of Tax Credit Certificates, and the Conditions for their Use, Revalidation and Transfer, Revenue Regulation No. 14-2011 [BIR Rev. Reg. No. 14-2011] (July 29, 2011).

transferred or assigned to any person.[104] Accordingly, the grantee-taxpayers of the TCC would be forced themselves to make use of the TCCs even if they do not have or have little tax liabilities or foreseeable tax liabilities with the BIR as opposed to having the option to transfer the TCCs to taxpayers with plenty of tax liabilities who would be able to maximize the use of the TCCs.

The regulation seems to have the effect of dissuading taxpayers from choosing the TCC option and indirectly encourages taxpayers to choose the cash refund option instead. In issuing RR No. 14-2011, the BIR recognizes the irregularities in the issuance and transfers of TCCs as well as difficulties in the monitoring of its use and transfer which may have caused huge revenue losses to government.[105] This is probably why the regulation disallowing the transfer of TCCs to any person was issued by the BIR.[106]

Although the regulation is beneficial to the government, the same is disadvantageous to the current holders of TCCs. Moreover, it violates the property right of the taxpayer to dispose of his property as owner and holder of the TCC.

It is to be noted that the TCC issued to any taxpayer already forms part of his property.[107] Article 428 of the Civil Code provides that "the owner has the right to enjoy and dispose"[108] his own properties. Further, the Constitution provides that "[n]o person shall be deprived of life, liberty, or property without due process of law."[109]

Considering that TCCs are valid claims of the taxpayer as a result of the taxpayer's excess taxes, the taxpayer should not be deprived of his right to make use of his assets in the way most beneficial to him.[110] The taxpayer should not be deprived of the option to sell or assign its TCCs to other taxpayers even at a discount.[111] Doing so violates the constitutional right to property of the taxpayer as owner and holder of the TCC in the sense that it restricts the taxpayer of his right to enjoy and dispose of his own property.[112]

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104. *Id.*

105. Lato, *supra* note 100.

106. *Id.*

107. *Id.*

108. An Act to Ordain and Institute the Civil Code of the Philippines [CIVIL CODE], Republic Act No. 386, art. 428 (1950).

109. PHIL. CONST. art. III, § 1.

110. Lato, *supra* note 100.

111. *Id.*

112. *Id.*

D. Payment of Value-Added Tax (VAT) and Excise Taxes on All Petroleum and Petroleum Products Imported Directly from Abroad to the Philippines, Including Freeport and Economic Zones

Section 106 (A) (2) (a) (5) of the National Internal Revenue Code provides that export sales such as those considered as "export sales under Executive Order No. 226, otherwise known as the Omnibus Investment Code of 1987, and other special laws" are subject to a zero percentage VAT rate.[113] This is elaborated further by RR No. 16-2005,[114] dated 1 September 2005, which provides that sales to export processing zones pursuant to R.A. Nos. 7916, as amended, 7903, 7922, and other similar export processing zones and "sale to enterprises duly registered and accredited with the Subic Bay Metropolitan Authority pursuant to R.A. 7227" are considered constructive export sales under Section 106 (A) (2) (a) (5) of the National Internal Revenue Code.[115]

Under R.A. No. 7916, otherwise known as the Special Economic Zone Act of 1995, [116] some of the fiscal and non-fiscal incentives granted to entities registered with the Philippine Economic Zone Authority (PEZA) are as follows: (1) Income tax holiday (ITH) for four years (six years for activities with pioneer status) which may be extended for a maximum period of three years subject to certain conditions; (2) After the ITH period, preferential tax of five percent based on gross income, which shall be in lieu of all local and national taxes; (3) During the ITH period, zero percent VAT on sales and on purchases of goods and services; (4) During the five percent tax regime, VAT exemption on sales and zero percent VAT on purchases of goods and services; and (5) Tax and duty free importation of capital equipment and raw materials, which are needed in the registered activity of the PEZA entity.[117]

113. TAX REFORM ACT OF 1997, § 106 (A) (2) (a).

114. Bureau of Internal Revenue, Consolidated Value-Added Tax Regulations of 2005, Revenue Regulation No. 16-2005 [BIR Rev. Reg. No. 16-2005] (Sep. 1, 2005).

115. *Id.* § 4.106-5.

116. An Act Providing for the Legal Framework and Mechanisms for the Creation, Operation, Administration, and Coordination of Special Economic Zones in the Philippines, Creating for this Purpose, the Philippine Economic Zone Authority (PEZA), and for Other Purposes [Special Economic Zone Act of 1995], Republic Act No. 7916, as Amended (1995).

117. *See* Triple I Consulting, PEZA Full Fiscal Incentives, *available at* http://www.tripleiconsulting.com/main/philippines-tax-incentive-programs/philippines-economic-zone-authorty-peza/peza-qualified-full-incentives/ (last accessed May 28, 2012).

RA No. 7227,[118] later amended by R.A. No. 9400,[119] provides for the same incentives, such that no national or local taxes shall be imposed on registered business enterprises within the Subic and Clark Freeport Zones, to wit —

> SECTION 12. Subic Special Economic Zone. —
>
> The abovementioned zone shall be subject to the following policies:
>
> ...
>
> (b) *The Subic Special Economic Zone shall be operated and managed as a separate customs territory ensuring free flow or movement of goods and capital within, into and exported out of the Subic Special Economic Zone, as well as provide incentives such as tax and duty-free importations of raw materials, capital and equipment.* However, exportation or removal of goods from the territory of the Subic Special Economic Zone to the other parts of the Philippine territory shall be subject to customs duties and taxes under the Customs and Tariff Code and other relevant tax laws of the Philippines;
>
> (c) The provisions of existing laws, rules and regulations to the contrary notwithstanding, *no taxes, local and national, shall be imposed within the Subic Special Economic Zone*[;]
>
> *In case of conflict between national and local laws with respect to tax exemption privileges in the Subic Special Economic Zone, the same shall be resolved in favor of the latter.*[120]

On 7 February 2012, the BIR issued RR No. 2-2012[121] which mandates the collection of "Value-Added and Excise taxes which are due on all petroleum and petroleum products that are imported and/or brought directly from abroad to the Philippines, including Freeport and Economic zones."[122] The same Regulation allows the oil companies to file a claim for credit or

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118. An Act Accelerating the Conversion of Military Reservations into Other Productive Uses, Creating the Bases Conversion and Development Authority for the Purpose, Providing Funds Therefore and for Other Purposes [Bases Conversion and Development Act of 1992], Republic Act No. 7227, as Amended (1992).

119. An Act Amending Republic Act No. 7227, as Amended, Otherwise Known as the Bases Conversion and Development Act of 1992, and for Other Purposes, Republic Act No. 9400 (2007).

120. Bases Conversion and Development Act of 1992, § 12 (emphasis supplied).

121. Bureau of Internal Revenue, Tax Administration of Petroleum and Petroleum Products Imported into the Philippines Including those Coming in Through Freeport Zones and Economic Zones and Registration of All Storage Tanks, Facilities, Depots and Terminals, Revenue Regulation No. 2-2012 [BIR Rev. Reg. No. 2-2012] (Feb. 7, 2012).

122. *Id.* § 3.

refund for the VAT and excise taxes paid on imported petroleum or petroleum products which are subsequently sold as zero-rated or exempt once they show proof to the BIR that the petroleum or petroleum products were sold and utilized within the freeport or economic zone.[123] The regulation also requires oil companies to register all their oil storage facilities, depots or terminals located within the freeport and economic zones with the "BIR Office having jurisdiction over said facilities."[124]

The Regulation was issued mainly to curb the "rampant smuggling of petroleum and petroleum products resulting to substantial revenue losses" and "to ensure the collection of taxes from whom they are due."[125] Although the Author empathizes with the BIR as to the rampant smuggling inside the freeport and economic zones of our country, it cannot be denied that the provisions of RR No. 2-2012 clearly contradict the provisions of R.A. No. 7916 and R.A. No. 7227. It is for this reason that on 4 April 2012, Judge Philbert I. Itturalde of the Regional Trial Court (RTC) of Pampanga issued a "writ of preliminary injunction, stopping the BIR from enforcing 'directly or indirectly' Revenue Regulation No. 2-2012 as it runs contrary to the law that created the Subic and Clark Freeport Zones" after a petition was filed by Pampanga solon Carmelo Lazatin.[126]

In his decision, Judge Iturralde ruled that "in order to prevent injury to the registered businesses inside [Clark Freeport Zone (CFZ)], there is a need to restrain the BIR from implementing Revenue Regulation No. 2-2012 until the main case has been heard."[127] Further, Judge Iturralde contradicted BIR's claim that the regulation merely intends to implement corrective measures to curb smuggling, to wit —

> 'A careful examination of the statute provides a penal sanction for such act,' Iturralde said, citing Section 9 of [R.A.] 9400, which states that '[a]ny registered business enterprise found guilty of smuggling by final judgment, either as principal, accomplice or accessory shall be perpetually barred from doing business in any freeport and special economic zone, in addition to the penalties and sanctions imposed by existing laws.'[128]

It is a basic requisite for validity that an administrative rule or regulation be reasonable and be within the scope and purview of the law it is

123. *Id.*

124. *Id.* § 4.

125. *Id.* background.

126. Reynaldo G. Navales, *Injunction vs revenue bureau's regulation issued*, SUN STAR PAMPANGA, Apr. 11, 2012, *available at* http://www.sunstar.com.ph/pampanga/local-news/2012/04/11/injunction-vs-revenue-bureau-s-regulation-issued215675 (last accessed May 28, 2012).

127. *Id.*

128. *Id.*

implementing. Administrative issuances, such as RR No. 2-2012, issued by the BIR, "must not override, supplant or modify the law."[129] Moreover, the Supreme Court in *Public Schools District Supervisors Association (PSDSA) v. De Jesus*[130] held —

> *The implementing rules and regulations of a law cannot extend the law or expand its coverage*, as the power to amend or repeal a statute is vested in the legislature. It bears stressing, however, that administrative bodies are allowed, under their power of subordinate legislation, to implement the broad policies laid down in the statute by 'filling in' the details. All that is required is that *the regulation be germane to the objectives and purpose of the law; that the regulation does not contradict but conforms with the standards prescribed by law.*[131]

RR No. 2-2012 tramples upon provisions of R.A. No. 7916 and R.A. No. 7227 which clearly provides that goods inside the freeport and economic zones should be tax and duty free. The latter laws provide that if an importer is located inside the freeport or economic zone, such importation shall not be subject to VAT and excise tax.[132] In addition, if the same importer sells such petroleum products within the freeport or economic zone, no tax shall be due.[133]

Even if RR No. 2-2012 provides that importers may seek for a tax refund of the VAT and excise taxes paid by them, the same regulation imposes the condition that the importers must properly show "to the satisfaction of the BIR" that the petroleum or petroleum products were consumed inside the Freeport or economic zone.[134] No particulars were mentioned in the regulation as to what is "sufficient evidence" satisfactory to the BIR.

It also cannot be denied that as a practice, claiming for a tax refund in our country usually takes a long time to prosper since this would require availability of cash funds on the part of the government. It should also be noted that in practice, tax refunds, which would require cash outflow from

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129. Romulo, Mabanta, Buenaventura, Sayoc, & De Los Angeles v. Home Development Mutual Fund, 333 SCRA 777, 786 (2000).

130. Public Schools District Supervisors Association (PSDSA) v. De Jesus, 491 SCRA 55 (2006).

131. *Id.* at 71 (citing National Tobacco Administration v. Commission on Audit, 311 SCRA 755, 770 (1999) & Sigre v. Court of Appeals, 387 SCRA 15, 23 (2002)) (emphasis supplied).

132. Rowena B. Bundang, Solons Seek Inquiry into BIR Issuance Regarding Oil Smuggling in Freeports and Ecozones, *available* at http://www.congress.gov.ph/press/details.php?pressid=6161 (last accessed May 28, 2012).

133. *Id.*

134. *See* BIR Rev. Reg. No. 2-2012, § 3.

the side of the government, are not usually prioritized by the BIR as opposed to the collection of taxes from taxpayers.

The Author cannot agree more with Mr. Danny J. Piano, President of the Subic Bay Freeport Chamber of Commerce, when he told the Subic Bay Updater in an interview that "it is very disconcerting that investors and locators are the ones who will be penalized and forced to take the brunt of additional bureaucracy when the solution to the problem simply lies in government agencies doing their jobs."[135]

RR No. 2-2012 issued by the BIR is not only burdensome, but is also overreaching as it goes beyond the scope and authority of the law legislated by the Philippine Congress. Such regulation should be voided.

House Representative of the First District of Pampanga, Carmelo F. Lazatin, warned that "if RR No. 2-2012 is upheld, it will set a dangerous precedent as the BIR can impose taxes on other and all importations by Freeport and Economic Locators"[136] and "would authorize the BIR to introduce amendments to R.A. 7227 which is a clear violation of the 1987 Constitution."[137]

E. Rulings Issued Prior to the National Internal Revenue Code of 1997 Shall No Longer Have Any Binding Effect

On 2 April 2012, the BIR issued RR No. 5-2012[138] which states that "[a]ll rulings issued prior to [1 January 1998] will no longer have any binding effect. Consequently, these rulings cannot be invoked as basis for any current business transaction/s. Neither can these rulings be used as a basis for securing legal tax opinions/rulings."[139] The rationale behind the regulation is stated in Section 1, in that owing to the numerous changes brought about by the implementation of R.A. No. 8424, most of the rulings issued prior to the said law are no longer applicable.[140]

The Regulation seems too drastic and overreaching, especially for taxpayers who seek to secure a legal tax opinion or ruling with the BIR. It should be noted that although there have been changes between the old Tax

135. Anthony Bayarong, *Subic locators cry foul over new BIR order*, PHIL. STAR, Mar. 7, 2012, *available at* http://www.philstar.com/nation/article.aspx?publicationsubcategoryid=200&articleid=784723 (last accessed May 28, 2012).

136. Bundang, *supra* note 132.

137. *Id.*

138. Bureau of Internal Revenue, Binding Effect of Rulings Issued Prior to Tax Reform Act of 1997, Revenue Regulation No. 5-2012 [BIR Rev. Reg. No. 5-2012] (Apr. 2, 2012).

139. *Id.* § 2.

140. *Id.* § 1.

Code of 1993 and the current National Internal Revenue Code of 1997, many or perhaps majority of the provisions in the old Tax Code have been carried over in the National Internal Revenue Code of 1997. It is unreasonable and unjust for the BIR to make a sweeping regulation when they themselves have acknowledged that only "most" of the rulings are no longer applicable. The BIR did not use "all" because they are fully aware that many of the BIR rulings issued prior to the National Internal Revenue Code of 1997 are still valid.

It would seem that the BIR is trying to make it more burdensome for taxpayers to secure a tax exemption or a preferential tax rate for their transactions by reducing the BIR rulings that they can use as basis when securing a tax opinion or ruling with the BIR.

If the BIR were indeed reasonable and fair, they would have made a conditional provision in RR No. 5-2012 such that only rulings issued prior to the National Internal Revenue Code of 1997 which are inconsistent with the current provisions of the National Internal Revenue Code of 1997 shall no longer have any binding effect. Rulings issued by the BIR prior to the National Internal Revenue Code of 1997 which are consistent with the current provisions of the National Internal Revenue Code of 1997 are deemed relevant and should still be applicable up to this time.

IV. VALIDITY OF THE RECENTLY ISSUED TAX RULES AND REGULATIONS

A. Consistency with the Law and the Constitution

It is a basic principle in administrative law that rules and regulations are promulgated by administrative authorities "only for the purpose of carrying out the provisions of the law into effect."[141] It must be stressed that "the power of administrative authorities to promulgate rules in the implementation of a statute is necessarily limited to what is provided for in the legislative enactment."[142] Such rules and regulations "cannot increase or decrease the requirements of the law, nor embrace matters not covered or intended to be covered by the statute."[143]

The BIR, in issuing the rules and regulations mentioned in Part III of this Article, among others, seem to have overstepped the letter, and more so, the spirit of the law it is trying to implement, supplement, and interpret it. There seems to be an insufficiency in reasoning and perhaps lack of basis in law and fact on the part of the BIR when they issued some of the rules and

141. NACHURA, *supra* note 19, at 393.

142. *Public Schools District Supervisors Association*, 491 SCRA at 71 (citing Blaquera v. Alcala, 295 SCRA 366, 436 (1998)).

143. DE LEON & DE LEON, JR., TAXATION, *supra* note 4, at 78 (citing 12 C.J.S. 845-46).

regulations. Such insufficiency has led taxpayers and tax practitioners to doubt why the BIR would suddenly change its position on a tax matter without adequate explanation and why the BIR would make such sweeping regulations which go against the provisions of laws which have long been enacted and enforced.

It should be noted that "the intent of the legislature is the controlling factor in the interpretation of the statute."[144] The BIR should bear this in mind as they continue to issue and implement new rules and regulations. The Author understands the goal of the BIR and respects its actions as the administrative agency tasked to assess and collect taxes in the Philippines for the support of the government. After all, "taxes are the lifeblood of the government."[145] However, the Author believes that there are just, reasonable, and legal means to carry out such goals.

Tax rules and regulations cannot restrict the scope of a statute, more so enlarge the scope of a statute.[146] Neither can they unjustly and prejudicially interfere with the personal and property rights of the people.[147] If they do, such rules and regulations should be voided.

The Author believes that one of the intentions of the National Internal Revenue Code is to attract foreign investors to our country. With the recently issued rulings and regulations which may be an onerous burden to investors, such as the requirement of filing a tax treaty relief application before availing of the preferential tax treaty rate as well as the payment of VAT and excise taxes on all petroleum and petroleum products imported directly from abroad to the Philippines, including freeport and economic zones, it is likely that many foreign investors will be discouraged to do business in our country.

B. Non-Retroactivity of Rulings

Even assuming for the sake of argument, that the recent rules and regulations have validly revoked the previous rulings and regulations on a particular tax matter, it should be noted that the same would have prejudicial effects to taxpayers, hence, should not have retroactive application. Section 246 of the National Internal Revenue Code provides —

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144. *Public Schools District Supervisors Association*, 491 SCRA at 82.

145. C. N. Hodges v. Municipal Board of the City of Iloilo, 7 SCRA 143, 147 (2006).

146. DE LEON & DE LEON, JR., ADMINISTRATIVE LAW, *supra* note 9, at 81 (citing 73 C.J.S. 413-14 & 416-17; *Toledo*, 202 SCRA at 507; *Luzon Polymers Corporation*, 209 SCRA at 71; *Comm. of Internal Revenue*, 240 SCRA at 368; *Republic*, 324 SCRA at 237; *Central Luzon Drug Corporation*, 456 SCRA at 414; & *MCC Industrial Sales Corp.*, 536 SCRA at 408).

147. DE LEON & DE LEON, JR., ADMINISTRATIVE LAW, *supra* note 9, at 82.

> SEC. 246. Non-Retroactivity of Rulings. — Any revocation, modification[,] or reversal of any of the rules and regulations promulgated in accordance with the preceding Section or any of the rulings or circulars promulgated by the Commissioner shall not be given retroactive application if the revocation, modification[,] or reversal will be prejudicial to the taxpayers, except in the following cases:
>
> (a) Where the taxpayer deliberately misstates or omits material facts from his return or in any document required by him by the [BIR];
>
> (b) Where the facts subsequently gathered by the [BIR] are materially different from the facts on which the ruling is based; or
>
> (c) Where the taxpayer acted in bad faith.[148]

In *ABS-CBN Broadcasting Corp. v. Court of Tax Appeals*,[149] dated 12 October 1981, the Supreme Court held that under Section 246 of the National Internal Revenue Code, the CIR is precluded from adopting a position contrary to one previously taken where injustice would result to taxpayer.[150] The Supreme Court has consistently reaffirmed in a long line of cases that BIR rulings have no retroactive effect where a grossly unfair deal would result to the prejudice of the taxpayer.[151]

V. CONCLUSION

The power to tax is believed to be the "strongest of all the powers of government."[152] However, it would be a fallacy to say that the power to tax, particularly the rule-making power of the BIR, is all-encompassing. No matter how broad the power of taxation is, it will always be subject to inherent and constitutional limitations. It is no wonder why the power of taxation is "sometimes called also as the power to destroy."[153] It can be a "destructive power which can interfere with the personal and property rights of the people and take[ ] from them a portion of their property for the support of the government."[154] Therefore, "it should be exercised with

148. TAX REFORM ACT OF 1997, § 246 (emphasis supplied).

149. ABS-CBN Broadcasting Corp. v. Court of Tax Appeals, 108 SCRA 142 (1981).

150. *Id.* at 151-52.

151. *See, e.g.*, Commissioner of Internal Revenue v. Burroughs Limited, 142 SCRA 324 (1986); Comm'r. of Internal Revenue v. Mega Gen. Mdsg. Corp., 166 SCRA 166 (1988); Commissioner of Internal Revenue v. Telefunken Semiconductor Philippines, Inc., 249 SCRA 401 (1995); & Commissioner of Internal Revenue v. Court of Appeals, 267 SCRA 557 (1997).

152. Hongkong & Shanghai Banking Corporation v. Rafferty, 39 Phil. 145, 150 (1918).

153. Roxas v. Court of Tax Appeals, 23 SCRA 276, 282 (1968).

154. Paseo Realty & Development Corporation v. Court of Appeals, 440 SCRA 235, 251 (2004).

caution to minimize the injury to the proprietary rights of a taxpayer. It must be exercised fairly, equally and uniformly, lest the tax collector kill the 'hen that lays the golden eggs.'"[155] Indeed, "[i]n order to maintain the general public's trust and confidence in the government, this power must be used justly and not treacherously."[156]

While the Author understands the goal and efforts of the BIR to generate revenue for the government and to improve the economy of the country, its actions should take into account its validity and reasonableness as well as its potential consequences in its entirety, lest we set them for nothing.

155. *Roxas*, 23 SCRA at 282.

156. *Id.*