

# Decode: Taxing the Digital Economy

*Anthony Mark A. Gutierrez\**

I. INTRODUCTION.....	1029
II. THE NATIONAL INTERNAL REVENUE CODE.....	1031
A. <i>History of E-Commerce</i>	
B. <i>The NIRC Through the Years</i>	
III. THE BIR ON TAXING E-COMMERCE.....	1035
IV. THE EIGHTEENTH CONGRESS ON TAXING E-COMMERCE.....	1037
V. THE CURRENT TAX REGIME .....	1038
A. <i>Income Tax Under the 1997 NIRC</i>	
B. <i>VAT Under the 1997 NIRC</i>	
C. <i>Online Business Transactions</i>	
D. <i>Underlying Transactions and Stakeholders</i>	
VI. TAX REGIMES IN OTHER JURISDICTIONS .....	1056
A. <i>Basic Legal Framework</i>	
B. <i>Enforcing Digital Tax</i>	
VII. THE WAY FORWARD .....	1062
A. <i>Income Tax</i>	
B. <i>VAT</i>	
C. <i>Tax Enforcement and Collection</i>	

---

\* '01 J.D. *class salutatorian*, Ateneo de Manila University School of Law. The Author is a founding partner of Gatmaytan Yap Patacsil Gutierrez & Protacio Law (C&G Law). He has been cited as a leading Philippine lawyer in the field of taxation by Chambers Asia Pacific in its 2010 to 2019 Asia-Pacific publications. The Legal 500 Asia Pacific likewise recognizes him as a leading lawyer in tax in its 2016 to 2019 publications.

## I. INTRODUCTION

Perhaps one of the biggest challenges of the living generation is surviving the COVID-19 pandemic. This coronavirus strain brought to humanity an unprecedented public health crisis in the 21st century.<sup>1</sup> As of 9 January 2021, a total of 218 countries have reported local transmission cases of the coronavirus, with more than 87 million confirmed cases and over a million deaths globally.<sup>2</sup> To curb the effects of the pandemic, governments of affected countries, with recommendations from the World Health Organization (WHO), epidemiologists, public health specialists, and the rest of the scientific community, imposed strict containment measures (e.g., lockdowns and community quarantines) in their respective jurisdictions to minimize the risk of spreading the virus.<sup>3</sup>

Commerce has been adversely affected. In the Philippines, it was reported that as of 29 April 2020, a total of 52.66% of registered Micro, Small and Medium Enterprises (MSMEs) have stopped their business operations due to the imposition of nationwide community quarantine.<sup>4</sup> The same period saw businesses and consumers reexamining and changing their production and consumption behaviors which, among others, led to a surge in transition to

- 
1. Organisation for Economic Co-operation and Development, Coronavirus (COVID-19): Joint actions to win the war, at 1, *available at* <https://www.oecd.org/about/secretary-general/Coronavirus-COVID-19-Joint-actions-to-win-the-war.pdf> (last accessed Jan. 8, 2021) [<https://perma.cc/FK49-MT59>].
  2. See World Health Organization, WHO Coronavirus Disease Dashboard, *available at* <https://covid19.who.int> (last accessed Jan. 8, 2021) [<https://perma.cc/M7TM-WLBB>].
  3. See World Health Organization, Coronavirus disease (COVID-19) advice for the public, *available at* <https://www.who.int/emergencies/diseases/novel-coronavirus-2019/advice-for-public> (last accessed Jan. 8, 2021) [<https://perma.cc/WW9P-FY6X>].
  4. Neil Arwin Mercado, *DTI: Over half of MSMEs in PH fully stopped operations due to virus outbreak*, PHIL. DAILY INQ., May 1, 2020, *available at* <https://business.inquirer.net/296227/dti-over-half-of-msmes-in-ph-fully-stopped-operations-due-to-virus-outbreak> (last accessed Jan. 8, 2021) [<https://perma.cc/5A6F-BMF9>].

online modalities of commerce.<sup>5</sup> The growth of online shopping was inevitable in a pandemic-stricken world. Some have reported that essentials and groceries were “being purchased in their platform on a click of 15[ ]times [ ] versus a normal pre-COVID[-19 time,]”<sup>6</sup> and they have recorded an increase in monthly orders compared to the period before the community quarantine was implemented.<sup>7</sup>

The loss of tax revenue caused by closed businesses made some of our lawmakers and tax authorities see the rise of electronic commerce (e-commerce) as an alternative source of government income.<sup>8</sup> This resulted in the government clarifying and revisiting the coverage of taxable transactions under the 1997 National Internal Revenue Code (1997 NIRC).<sup>9</sup> The House of Representatives Committee on Ways and Means, for instance, has approved a 12% value-added tax (VAT) on digital transactions on third party platform providers which act as conduit for goods and services, and suppliers of digital services.<sup>10</sup> Meanwhile, the Bureau of Internal Revenue (BIR) issued Revenue Memorandum Circular No. 60-2020 (RMC No. 60-2020)<sup>11</sup> reminding persons doing business and earning income, specifically those who are into

- 
5. Angela Clarino, *Covid caused ‘massive change in consumer behavior’, says online shopping service*, MANILA TIMES, July 30, 2020, available at <https://www.manilatimes.net/2020/07/30/news/latest-stories/covid-caused-massive-change-in-consumer-behavior-says-online-shopping-service/748218> (last accessed Jan. 8, 2021) [<https://perma.cc/2CRL-HFL2>].
  6. *Id.*
  7. *Id.*
  8. An Act Establishing a Fiscal Regime for the Digital Economy, Amending for the Purpose Sections 57, 105, 108, and 114 of the National Internal Revenue Code, and for Other Purposes, H.B. No. 6765, explan. n., 18th Cong., 1st Reg. Sess. (2020).
  9. An Act Amending the National Internal Revenue Code, as Amended, and for Other Purposes [NAT’L INTERNAL REVENUE CODE OF 1997], Republic Act No. 8424 (1997) (as amended).
  10. Ralf Rivas, *House panel approves 12% ‘Netflix, Lazada’ tax*, RAPPLER, July 29, 2020, available at <https://www.rappler.com/business/house-panel-approves-tax-digital-transactions> (last accessed Jan. 8, 2021) [<https://perma.cc/QN7H-P3PG>].
  11. Bureau of Internal Revenue, *Obligations of Persons Conducting Business Transactions Through Any Forms of Electronic Media, and Notice to Unregistered Businesses*, Revenue Memorandum Circular No. 60-2020 [RMC No. 60-2020] (June 10, 2020).

digital transactions, to ensure business registration pursuant to Section 236 of the 1997 NIRC.<sup>12</sup>

These recent attempts to seemingly cover digital services and online selling platforms in tax laws have apparently caused some confusion among the public.<sup>13</sup> Some quarters expressed that the tax imposition was ill-timed, considering the financial struggles many are experiencing in the middle of the pandemic.<sup>14</sup> The BIR clarified that its recent move for the enforcement of tax liabilities on e-commerce is primarily intended against giant online selling platforms and digital services providers, and not against small-time online sellers.<sup>15</sup>

This Article will examine the current taxation regime which may be applicable to e-commerce and online business transactions in the Philippines, as well as the proposals pending in Congress and BIR issuances in relation to online business transactions. This Article will also look at taxation models for online business transactions adopted in other jurisdictions.

## II. THE NATIONAL INTERNAL REVENUE CODE

### *A. History of E-Commerce*

Before currency was invented, people resorted to exchanging of goods, properties, and services — otherwise known as bartering.<sup>16</sup> As technology and civilization advanced, people used money and other forms of currency, usually with a piece of paper which is worthless in itself but is given value by society.<sup>17</sup> Variations of trading using money in exchange of goods and services were formed, paving the way for modern-day commercial transactions.

---

12. *Id.* para. 1.

13. Leila B. Salaverria, *BIR targeting Netflix, Lazada, not small-time online sellers*, PHIL. DAILY INQ., June 18, 2020, available at <https://business.inquirer.net/300201/bir-targeting-netflix-lazada-not-small-time-online-sellers> (last accessed Jan. 8, 2021) [<https://perma.cc/7HGR-W5Z6>].

14. *Id.*

15. *Id.*

16. Square, *The History of Trade and Barter System*, available at <https://squareup.com/us/en/townsquare/a-history-of-the-trade-and-barter-system> (last accessed Jan. 8, 2021) [<https://perma.cc/V9HD-2RB7>].

17. *Id.*

In the 1960s, the use of the Advanced Research Projects Agency Network (ARPANET)<sup>18</sup> enabled the circulation of military information among different places in case of a possible nuclear attack.<sup>19</sup> The ARPANET used packet switching to allow multiple computers to communicate on a single network.<sup>20</sup> Sometime in 1983, ARPANET eventually adopted the internet communications model (TCP/IP) and was developed to enable fast transmission of data between multiple networks.<sup>21</sup> The same communications model is still being used until today, although with more advancements to data transfer speed, security, and accessibility.<sup>22</sup>

The internet arrived in the Philippines at around March 1994 when the first permanent public connection through a 64 kbit/s link to Sprint, an American internet service provider (ISP), was established.<sup>23</sup> The Philippines was able to commercially launch the internet available to the public sometime in August 1994, through Mosaic Communications.<sup>24</sup> Internet access became the impetus for having business online transactions in the Philippines. As the internet connection in the Philippines improved, in 2006, Filipino entrepreneurs developed *Sulit.com.ph*, the first fully functioning buy-and-sell

- 
18. Evan Andrews, Who invented the internet?, *available at* <https://www.history.com/news/who-invented-the-internet> (last accessed Jan. 8, 2021) [<https://perma.cc/ZVS2-8C6U>].
  19. Cade Metz & Paul Baran, the link between nuclear war and the internet, *available at* <https://www.wired.co.uk/article/h-bomb-and-the-internet> (last accessed Jan. 8, 2021) [<https://perma.cc/8R89-Q8NY>].
  20. Andrews, *supra* note 18.
  21. *Id.*
  22. Avast Academy, What is TCP/IP and How Does it Work?, *available at* <https://www.avast.com/c-what-is-tcp-ip> (last accessed Jan. 8, 2021) [<https://perma.cc/3FQP-3PSN>].
  23. Michael Minges, et al., Pinoy Internet: Philippines Case Study, at 22, *available at* [https://www.academia.edu/2292795/Pinoy\\_Internet\\_Philippines\\_Case\\_Study](https://www.academia.edu/2292795/Pinoy_Internet_Philippines_Case_Study) (last accessed Jan. 8, 2021) [<https://perma.cc/Z2SV-5D88>] (citing Miguel A. L. Paraz, Developing a Viable Framework for Commercial Internet Operations in the Asia-Pacific Region: The Philippine Experience, *available at* [https://web.archive.org/web/20160103124914/https://www.isoc.org/inet97/proceedings/E6/E6\\_1.HTM](https://web.archive.org/web/20160103124914/https://www.isoc.org/inet97/proceedings/E6/E6_1.HTM) (last accessed Jan. 8, 2021) [<https://perma.cc/9A3C-UZ5Z>]).
  24. Minges, et al., *supra* note 23, at 22.

website.<sup>25</sup> Online selling of goods grew as internet connection became faster and more stable. By 2011, the social networking site *Multiply*, which was initially intended as a network website to connect people around the world, was used by Filipino merchants as their free online platform in selling their goods and services, so much so that *Multiply* eventually shifted to a full e-commerce website.<sup>26</sup> After series of mergers, closures, and acquisition of companies, the current big players in the Philippines which offer online platforms for buy-and-sell are *Lazada* and *Shopee*.<sup>27</sup>

### B. The NIRC Through the Years

When the first NIRC (1939 NIRC) took effect in July 1939,<sup>28</sup> the internet did not yet exist.<sup>29</sup> At the time Presidential Decree No. 1158-A, s. 1977 (1977 NIRC)<sup>30</sup> was enacted to amend the 1939 NIRC, the ARPANET was in

- 
25. See Startup Grind, RJ David (Sulit.com.ph), available at <https://www.startupgrind.com/events/details/startup-grind-manila-hosted-rj-david-sulit-com-ph> (last accessed Jan. 8, 2021) [<https://perma.cc/6X3K-VHCM>] & ABS-CBN News, *Meet the Filipino couple behind Sulit.com.ph*, ABS-CBN NEWS, Apr. 22, 2013, available at <https://news.abs-cbn.com/business/04/22/13/meet-filipino-couple-behind-sulitcomph> (last accessed Jan. 8, 2021) [<https://perma.cc/EH6F-PFBB>].
26. Therese Reyes, *INFOGRAPHIC: Fast facts on Online Shopping in PH*, RAPPLER, May 31, 2016, available at <https://www.rappler.com/brandrap/finance-and-industries/ecommerce-industry-philippines> (last accessed Jan. 8, 2021) [<https://perma.cc/9PYL-84XA>].
27. Annelle Tayao-Juego, *Lazada, Shopee, ZALORA top list of most visited online stores in PH*, PHIL. DAILY INQ., Apr. 3, 2020, available at <https://business.inquirer.net/293997/lazada-shopee-zalora-top-list-of-most-visited-online-stores-in-ph> (last accessed Jan. 8, 2021) [<https://perma.cc/H6U6-ZCHN>].
28. An Act to Revise, Amend, and Codify the Internal Revenue Laws of the Philippines [NAT'L INTERNAL REVENUE CODE], Commonwealth Act No. 466 (1939).
29. Andrews, *supra* note 18.
30. Amending Certain Sections of the National Internal Revenue Code of 1939 for Incorporation in the Consolidation and Codification of All Existing Revenue Laws Under a Presidential Decree No. 1158, Presidential Decree No. 1158-A (1977).

place, but the internet communications model (TCP/IP) was not yet available.<sup>31</sup>

When the 1997 NIRC took effect,<sup>32</sup> the Philippines already had commercial access to the internet, although internet connection was not stable and secure enough to host selling platforms.<sup>33</sup> It was only several years later when online business transactions through selling platforms like *Sulit* and *Multiply* became prevalent.<sup>34</sup>

In June 2000, Republic Act No. 8792,<sup>35</sup> otherwise known as the Electronic Commerce Act of 2000, was enacted. This law defined service providers as those providers of “[online] services or network access or the operator of facilities therefor, including entities offering the transmission, routing, or providing of connections for online communications, digital or otherwise, between or among points specified by a user, of electronic documents of the user’s choosing.”<sup>36</sup> The law also recognized electronic data messages, electronic documents, and electronic signatures.<sup>37</sup>

Around 20 years from the effectivity of the 1997 NIRC, the Tax Reform for Acceleration and Inclusion Law (TRAIN Law),<sup>38</sup> took effect. The TRAIN Law introduced various amendments to the 1997 NIRC, although

---

31. Andrews, *supra* note 18.

32. Republic Act No. 8424 was previously called the Tax Reform Act of 1997 before its amendment.

33. Minges, et al., *supra* note 23, at 25.

34. Reyes, *supra* note 26.

35. An Act Providing for the Recognition and Use of Electronic Commercial and Non-Commercial Transactions, Penalties for Unlawful Use Thereof, and Other Purposes [Electronic Commerce Act], Republic Act No. 8792 (2000).

36. *Id.* § 5 (i).

37. *Id.* §§ 6-8.

38. An Act Amending Sections 5, 6, 24, 25, 27, 31, 32, 33, 34, 51, 52, 56, 57, 58, 74, 79, 84, 86, 90, 91, 97, 99, 100, 101, 106, 107, 108, 109, 110, 112, 114, 116, 127, 128, 129, 145, 148, 149, 151, 155, 171, 174, 175, 177, 178, 179, 180, 181, 182, 183, 186, 188, 189, 190, 191, 192, 193, 194, 195, 196, 197, 232, 236, 237, 249, 254, 264, 269, and 288; Creating New Sections 51-A, 148-A, 150-A, 150-B, 237-A, 264-A, 264-B, and 265-A; and Repealing Sections 35, 62, and 89; All Under Republic Act No. 8424, Otherwise Known as the National Internal Revenue Code of 1997, as Amended, and for Other Purposes [Tax Reform for Acceleration and Inclusion (TRAIN)], Republic Act No. 10963 (2017).

none was specifically related to online business transactions.<sup>39</sup> Notably, in 2015, it is reported that there were 26.01 million e-commerce users in the Philippines,<sup>40</sup> and in the first quarter of 2017, the Philippines had an average broadband internet connection speed of 5.5 megabits per second (Mbps)<sup>41</sup> and an average mobile internet connection speed of 8.7 Mbps.<sup>42</sup>

### III. THE BIR ON TAXING E-COMMERCE

More than six years before the COVID-19 pandemic broke out, sometime in August 2013, the BIR issued Revenue Memorandum Circular No. 55-2013 (RMC No. 55-2013)<sup>43</sup> which recognized that “[a]n increasing number of consumers are visiting and purchasing goods and services from ... online stores primarily because of the high level of convenience inherent in online shopping which can be done within the confine of one’s home, office, and even in public places offering internet access.”<sup>44</sup>

RMC No. 55-2013 reminded “parties in ... online business transactions of their tax obligations.”<sup>45</sup> RMC No. 55-2013 stated that

existing tax laws and revenue issuances on the tax treatment of purchases (local or imported) and sale (local or international) of goods (tangible or intangible) or services shall be equally applied with no distinction on whether or not the marketing channel is the internet/digital media or the typical and customary physical medium.<sup>46</sup>

---

39. *Id.*

40. Reyes, *supra* note 26.

41. Victor Barreiro, Jr., *PH has slowest average internet speed in Asia Pacific — report*, RAPPLER, June 1, 2017, available at <https://www.rappler.com/technology/philippines-akamai-broadband-adoption-internet-speed-rankings> (last accessed Jan. 8, 2021) [<https://perma.cc/7D4K-RBZ3>].

42. Akamai, Q1 2017 executive summary, at 4, available at <https://www.akamai.com/us/en/multimedia/documents/state-of-the-internet/q1-2017-state-of-the-internet-connectivity-executive-summary.pdf> (last accessed Jan. 8, 2021) [<https://perma.cc/DWE5-6R6B>].

43. Bureau of Internal Revenue, *Reiterating Taxpayers’ Obligations in Relation to Online Business Transactions*, Revenue Memorandum Circular No. 55-2013 [RMC No. 55-2013] (Aug. 5, 2013).

44. *Id.* at 1.

45. *Id.*

46. *Id.* at 3.



Hence, “[l]ike any other business establishments, persons who conduct business through ... online transactions ... have the obligations to.”<sup>47</sup>

- (1) “Register the business at the Revenue District Office (RDO)[;]”<sup>48</sup>
- (2) “Secure the required Authority to Print (ATP) invoices/receipts and register books of accounts for use in business[;]”<sup>49</sup>
- (3) “Issue registered invoice or receipt[;]”<sup>50</sup>
- (4) “Withhold [and remit] required creditable/expanded withholding tax, final tax, tax on compensation of employees, and other withholding taxes[;]”<sup>51</sup>
- (5) “File applicable tax returns on or before the due dates, pay correct internal revenue taxes, and submit information returns and other tax compliance reports[; and]”<sup>52</sup>
- (6) “Keep books of accounts and other business/accounting records[.]”<sup>53</sup>

On 1 June 2020, the BIR issued RMC No. 60-2020 to reiterate the obligation of

all persons doing business and earning income in any manner or form, specifically those who are into digital transactions through the use of any electronic platforms and media, and other digital means, to ensure that their businesses are registered pursuant to Section 236 of the Tax Code, as amended[,] and that they are tax compliant.<sup>54</sup>

RMC 60-2020 expressly referred to “not only partner sellers/merchants, but also other stakeholders involved such as payment gateways, delivery channels, internet service providers, and other facilitators.”<sup>55</sup>

---

47. *Id.* at 2.

48. *Id.*

49. RMC No. 55-2013, at 2.

50. *Id.*

51. *Id.* at 3.

52. *Id.*

53. *Id.*

54. RMC No. 60-2020, para. 1.

55. *Id.*

## IV. THE EIGHTEENTH CONGRESS ON TAXING E-COMMERCE

In a span of four months since the community quarantine began in March 2020,<sup>56</sup> at least three bills were filed with the House of Representatives specifically dealing with taxing the digital economy.

*First*, House Bill No. 6765 (H.B. No. 6765)<sup>57</sup> was submitted to the House of Representatives Committee on Ways and Means on 19 May 2020. The bill essentially seeks to: (1) make network orchestrators withholding agents for income taxes and VAT, (2) clarify that services rendered electronically in the course of trade or business are subject to VAT, and (3) require digital service providers to provide services through a resident agent or representative in the Philippines.<sup>58</sup>

*Second*, House Bill No. 6944 (H.B. No. 6944),<sup>59</sup> which was filed on 3 June 2020, intends to legislate a new tax in the form of digital tax of six percent on the gross sales to consumers in the Philippines imposed on digital service providers.<sup>60</sup>

*Third*, House Bill No. 7425 (H.B. No. 7425)<sup>61</sup> was submitted to the House of Representatives Committee on Ways and Means on 18 August 2020 as a substitute bill for H.B. Nos. 6765 and 6944.<sup>62</sup> The key provisions of H.B. No. 7425 aim to: (1) “[clarify] the imposition of VAT on electronic or online sale of services[,]”<sup>63</sup> (2) “[define] the liable digital service provider (DSP)[.]”<sup>64</sup> and

---

56. Office of the President, Community Quarantine Over the Entire Luzon and Further Guidelines for the Management of the Coronavirus Disease 2019 (COVID-19) Situation, at 1 (Mar. 16, 2020).

57. H.B. No. 6765.

58. *Id.* explan. n.

59. An Act Establishing Digital Taxation in the Philippines, H.B. No. 6944, 18th Cong., 1st Reg. Sess. (2020).

60. *Id.* § 4.

61. An Act Imposing Value-Added Tax on Digital Transactions in the Philippines Amending for the Purpose Section 105, 108, 109, 110, 113, 114, and 236 and Adding a New Section 105-A of the National Internal Revenue Code of 1997, As Amended, H.B. No. 7425, 18th Cong., 1st Reg. Sess. (2020).

62. Committee on Ways and Means, H. Comm. Rep. No. 426, at \*2, 18th Cong., 2d Reg. Sess. (2020).

63. *Id.* at \*17.

64. *Id.*

(3) “[require] non[-]resident DSPs to collect and remit the VAT[,] among others.”<sup>65</sup>

## V. THE CURRENT TAX REGIME

Questions have been raised whether online business transactions are subject to income and value-added tax under the 1997 NIRC. This Chapter examines the existing tax regime, identifies the typical online business transactions and stakeholders involved, and analyzes which stakeholders and transactions are subject to Philippine income tax and VAT.

### A. Income Tax Under the 1997 NIRC

Taxable income is the “pertinent items of gross income ... less deductions, if any.”<sup>66</sup> Gross income, in turn, means “all income derived from whatever source.”<sup>67</sup>

Section 32 of the 1997 NIRC enumerates certain types of income that may be subject to income tax, but it also states that income shall “not [be] limited” to the items enumerated.<sup>68</sup> In the words of the Supreme Court, income generally means “profits or gains.”<sup>69</sup> Further —

[I]ncome may be defined as an amount of money coming to a person or corporation within a specified time, whether as payment for services, interest[,] or profit from investment. Unless otherwise specified, it means cash or its equivalent. Income can also be though[t] of as [a] flow of the fruits of one’s labor.<sup>70</sup>

---

65. *Id.* at \*18.

66. NAT’L INTERNAL REVENUE CODE OF 1997, § 31 (as amended).

67. *Id.* § 32 (A).

68. *Id.*

69. *Madrigal v. Rafferty*, 38 Phil. 414, 419 (1918) (citing *London County Council v. Attorney-General*, 5 T.C. 242 (1903-1911) (U.K.)). *See also* THOMAS GOLD, A TREATISE ON THE FEDERAL INCOME TAX UNDER THE ACT OF 1913 13 (1915); DUNCAN BLACK, THE INCIDENCE OF INCOME TAXES (1915); *Gibbons v. Mahon*, 136 U.S. 549 (1890); & *Towne v. Eisner*, 245 U.S. 418 (1918)).

70. *Conwi v. Court of Tax Appeals*, G.R. No. 48532, 213 SCRA 83, 87-88 (1992) (citing *Fisher v. Trinidad*, 43 Phil. 973, 981 (1922) & *Madrigal*, 38 Phil. at 418)).

The Supreme Court and the Court of Tax Appeals have declared that the definition of gross income is “broad and comprehensive”<sup>71</sup> to include proceeds from activities not enumerated in the law.<sup>72</sup>

For example, in *Chamber of Real Estate and Builders’ Association, Inc. v. Romulo*,<sup>73</sup> the Supreme Court held that

[i]ncome means all the wealth which flows into the taxpayer other than a mere return on capital. Capital is a fund or property existing at one distinct point in time while income denotes a flow of wealth during a definite period of time. Income is gain derived and severed from capital.<sup>74</sup>

The Supreme Court also identified elements in determining when an income is taxable. These are: “(1) there must be [a] gain[,] (2) the gain must be realized or received[,] and (3) the gain must not be excluded by law or treaty from taxation.”<sup>75</sup>

In *Commissioner of Internal Revenue v. British Overseas Airways Corp.*,<sup>76</sup> it was held that “the words ‘income from any source whatever’ discloses a legislative policy to include all income not expressly exempted within the class of taxable income under our laws.”<sup>77</sup>

Under the Philippine regime of income taxation, income derived by resident citizens and domestic corporations from all sources, whether within or without of the Philippines, shall be taxable;<sup>78</sup> while only income derived within the Philippines by non-resident citizens, aliens, and foreign corporations shall be taxable.<sup>79</sup> It is in the latter instances which typically

---

71. *Commissioner of Internal Revenue v. British Overseas Airways Corp.*, G.R. No. L-65773-74, 149 SCRA 395, 406 (1987).

72. *Id.* at 406-07.

73. *Chamber of Real Estate and Builders’ Association, Inc. v. Romulo*, G.R. No. 160756, 614 SCRA 605 (2010).

74. *Id.* at 627 (citing *Madrigal*, 38 Phil. at 418 & *Commissioner of Internal Revenue v. Court of Appeals*, G.R. No. 108576, 301 SCRA 152, 173 (1999)).

75. *Chamber of Real Estate and Builders’ Association, Inc.*, 614 SCRA at 627 (citing *Commissioner of Internal Revenue*, 301 SCRA at 181).

76. *Commissioner of Internal Revenue v. British Overseas Airways Corporation*, G.R. No. L-65773-74, 149 SCRA 395 (1987).

77. *Id.* at 406-07.

78. NAT’L INTERNAL REVENUE CODE OF 1997, § 23 (A) & (E).

79. *Id.* § 23 (B), (D), & (F).

prompt the question whether a particular type of income is Philippine-sourced and subject to Philippine taxes.

The basic rules on situs of taxation are found in Section 42 of the NIRC.<sup>80</sup> In essence, compensation for labor or personal services performed in the Philippines shall be deemed as income from sources within the Philippines,<sup>81</sup> while gains, profits, and income from sale of personal property within the Philippines shall be treated as derived entirely within the Philippines.<sup>82</sup>

The list of different types of income under Section 42 of the 1997 NIRC mentions: (1) interests, (2) dividends, (3) services, (4) rentals and royalties, (5) sale of real property, and (6) sale of personal property;<sup>83</sup> although the enumeration is not considered exclusive, and income not mentioned in the list may still be deemed sourced within the Philippines.<sup>84</sup> In *British Traders' Insurance Co., Ltd. v. Commissioner of Internal Revenue*,<sup>85</sup> the Supreme Court declared that "Section 37 [now Section 42 of the 1997 NIRC] is obviously not an all-inclusive enumeration, for it only directs that the types of income mentioned therein be treated as income from sources within the Philippines, but does not state that no other kind of income be likewise so considered."<sup>86</sup> "The test of taxability is the 'source[,] and the source of an income is that activity ... which produced the income."<sup>87</sup> The word "source" conveys the idea of "origin."<sup>88</sup>

#### B. VAT Under the 1997 NIRC

Section 105 of the 1997 NIRC states that, "[a]ny person who, in the course of trade or business, sells, barter[s], exchange[s], lease[s] goods or properties, renders

---

80. *Id.* § 42.

81. *Id.* § 42 (A) (3).

82. *Id.* § 42 (A) (6) & (E).

83. *Id.* § 42 (A).

84. See *British Overseas Airways Corp.*, 149 SCRA at 406-07.

85. *British Traders' Insurance Co., Ltd. v. Commissioner of Internal Revenue*, G.R. No. L-20501, 13 SCRA 719 (1965).

86. *Id.* at 725.

87. *British Overseas Airways Corporation*, 149 SCRA at 408 (citing *Alexander Howden & Co., Ltd. v. Collector of Internal Revenue*, G.R. No. L-19392, 13 SCRA 601, 604 (1965)).

88. *Manila Gas Corp. v. Collector of Internal Revenue*, 62 Phil. 895, 901 (1936).

services, and any person who imports goods shall be subject to the value-added tax ... .”<sup>89</sup>

The BIR’s Revenue Regulations No. 16-2005 (RR No. 16-2005)<sup>90</sup> characterized VAT as

a tax on consumption levied on the sale, barter, exchange or lease of goods or properties and services in the Philippines and on importation of goods into the Philippines. The seller is the one statutorily liable for the payment of the tax, but the amount of the tax may be shifted or passed on to the buyer, transferee or lessee of the goods, properties or services. ... However, in the case of importation, the importer is the one liable for the VAT.<sup>91</sup>

VAT is considered a transaction tax — it is imposed on sales, barter, exchanges of goods or property, and on the performance of services,<sup>92</sup> and “is a tax on consumption ‘expressed as a percentage of the value added to goods or services’ purchased by the producer or taxpayer.”<sup>93</sup>

The VAT system also adheres to the *destination principle*, which means that goods and services are taxed in the country where these are consumed.<sup>94</sup> “Consumption is ‘the use of a thing in a way that thereby exhausts it.’ Applied to services, the term means the performance or ‘successful completion of a contractual duty, usually resulting in the performer’s release from any past or future liability.’”<sup>95</sup> In *Commissioner of Internal Revenue v. American Express*

---

89. NAT’L INTERNAL REVENUE CODE OF 1997, § 105.

90. Bureau of Internal Revenue, Consolidated Value-Added Tax Regulations of 2005, Revenue Regulation No. 16-2005 [RR No. 16-2005] (Sept. 1, 2005).

91. *Id.* § 4.105-2.

92. *Commissioner of Internal Revenue v. Negros Consolidated Farmers Multi-Purpose Cooperative*, G.R. No. 212735, 888 SCRA 402, 424 (2018).

93. *Commissioner of Internal Revenue v. American Express International, Inc.*, G.R. No. 152609, 462 SCRA 197, 215 (2005) (citing VICTOR A. DEOFERIO & VICTORINO C. MAMALATEO, *THE VALUE ADDED TAX IN THE PHILIPPINES* (2000) & ROBERT SELLERS SMITH, *WEST’S TAX LAW DICTIONARY* 892 (1993)).

94. *Atlas Consolidated Mining and Development Corp. v. Commissioner of Internal Revenue*, G.R. No. 141104, 524 SCRA 73, 102-03 (2007) (citing *Commissioner of Internal Revenue v. Seagate Technology (Philippines)*, G.R. No. 153866, 451 SCRA 132, n. 53 (2005)).

95. *American Express International, Inc.*, 462 SCRA at 217 (citing BLACK’S LAW DICTIONARY 336 & 1173 (7th ed. 1999)).

*International, Inc.*,<sup>96</sup> the Supreme Court held that “[u]nlike goods, services cannot be physically used in or bound for a specific place when their destination is determined. Instead, there can only be a ‘predetermined end of a course’ when determining the service ‘location or position ... for legal purposes.’”<sup>97</sup>

In general, to determine whether a transaction is subject to VAT, there must be a transaction involving sale of goods or services within, or importation into, the Philippines.<sup>98</sup>

### C. Online Business Transactions

RMC No. 55-2013 enumerates four common types of online business transactions in the Philippines, namely: (1) online shopping or online retailing, (2) online intermediary service, (3) online advertisement/classified ads, and (4) online auction.<sup>99</sup> RMC No. 55-2013 defined them as follows:

- (1) Online shopping or online retailing ... is a form of electronic commerce whereby consumers directly buy goods or services from a seller over the internet without an intermediary service. An online shop, e-shop, e-store, internet shop, web shop, web store, online store, or virtual store evokes the physical analogy of buying products or services at a bricks-and-mortar-retailer or shopping center.
- (2) Online intermediary service ... is a third party that offers intermediation services between two trading parties. The intermediary acts as a conduit for goods or services offered by a supplier to a consumer and receives commission therefor. In this case, the relationship between the intermediary and the merchant shall be that of a principal-agent relationship which shall be governed by their agreement including but not limited to the amount of commission, manner of transmitting the same, etc.

...

- (3) Online advertisement ... is a form of promotion that uses the internet to deliver marketing messages to attract customers.

---

96. *Commissioner of Internal Revenue v. American Express International, Inc.*, G.R. No. 152609, 462 SCRA 197 (2005).

97. *Id.* at 217 (citing BLACK’S LAW DICTIONARY 479 & 1421).

98. NAT’L INTERNAL REVENUE CODE OF 1997, §§ 106 (A); 107 (A) (as amended); & 108 (A).

99. RMC No. 55-2013, at 1-2.

- (4) Online auctions ... are auctions conducted through the internet via an online service provider that specifically hosts such auctions. Through this service, the seller sells the product or service to the person who bids the highest price.<sup>100</sup>

RMC No. 55-2013 states that

[t]he existing tax laws and revenue issuances on the tax treatment of purchases (local or imported) and sale (local or international) of goods (tangible or intangible) or services shall be equally applied with no distinction on whether or not the marketing channel is the internet/digital media or the typical and customary physical medium.<sup>101</sup>

#### *D. Underlying Transactions and Stakeholders*

##### *I. Online Shopping or Online Retailing*

As referred to in RMC No. 55-2013, online shopping or online retailing involves “consumers directly buying goods or services from a seller over the internet without an intermediary service.”<sup>102</sup> The transaction usually involves a seller, a buyer, and possibly a payment gateway,<sup>103</sup> and a logistics service provider for the delivery of the goods from the seller to the consumer-buyer.<sup>104</sup> A seller may either be within or outside of the Philippines, and the goods may either be tangible or intangible.<sup>105</sup>

The underlying taxable activities typically involved in an online shopping or online retailer transaction are: (a) the sale of goods or services between the

---

100. *Id.*

101. *Id.* at 3.

102. *Id.* at 1.

103. RMC No. 55-2013 states —

*Payment gateways or payment settlement entities* refer to banks or other organizations and third party settlement organizations that has (*sic*) contractual obligation to make payment to participating payees in the settlement of the transactions. These include, but are not limited to, credit card companies, banks, financial institutions, and bill paying services.

*Id.* at 4.

104. *Id.* at 2. Unless stated otherwise, this Article assumes that the buyers are in the Philippines.

105. RMC No. 55-2013, at 3.



seller and the buyer, (b) the service provided by the payment gateway, and (c) the service performed by a logistics provider.<sup>106</sup>

In both the sale of goods and performance of services, income may be derived from the conduct of trade or business. This income would form part of the gross income derived from the conduct of trade or business.<sup>107</sup> In turn, the gross income may potentially give rise to a taxable income after deductions are made pursuant to Section 31 of the NIRC.<sup>108</sup>

Even though online transactions are made through the internet without any of the stakeholders having possibly seen or verbally communicated with each other, the underlying transactions involved are no different from the buy-and-sell activities which people have been doing since commerce began. The medium in which the transaction was negotiated and consummated (i.e., were conducted online) does not appear to alter the essence of the transactions. The sale of goods online, for example, could still fall under the category of a contract of sale, whereby “one of the contracting parties obligates himself to transfer the ownership of and to deliver a determinate thing, and the other to pay therefor a price certain in money or its equivalent.”<sup>109</sup>

*a. Income Tax*

In terms of income taxation, the medium in conducting transactions does not appear to be sufficient reason to characterize online sales transactions differently from sales consummated in brick-and-mortar stores, markets and malls. The phrase “income from any source whatever” under Section 32 of the 1997 NIRC discloses “a legislative policy to include all income not expressly exempted within the class of taxable income.”<sup>110</sup> Thus, regardless of how a sale is transacted, whether through an online platform or not, the income generated may be subject to income tax.

Nevertheless, it is important to distinguish sellers and logistics providers who are non-resident citizens, aliens, or foreign corporations who have no physical presence in the Philippines. This is because, under our system of

---

106. *Id.* at 3-4.

107. NAT'L INTERNAL REVENUE CODE OF 1997, § 32 (A) (2).

108. *Id.* § 31 (as amended).

109. An Act to Ordain and Institute the Civil Code of the Philippines [CIVIL CODE], Republic Act No. 386, art. 1458 (1949).

110. *British Overseas Airways Corp.*, 149 SCRA at 406-07.

income taxation, the generation of income itself does not automatically make it taxable under Philippine law.<sup>111</sup>

For sellers and service providers who are resident citizens and domestic corporations and sell goods and services online (referred to as onshore sellers), the question of liability may not be that difficult to answer because under our income tax system, income they derive within and outside the Philippines is subject to income tax.<sup>112</sup> The question may become complex when a seller or service provider is a non-resident citizen, alien or foreign corporation who sells goods and services online but has no physical presence in the Philippines (referred to as offshore sellers). This is because income from sale of property or performance of a service shall be subject to income tax only when the income is sourced within the Philippines.<sup>113</sup>

It is also essential to properly characterize whether the online transaction involves a service or a sale of personal property because the situs rules are different.

Generally, under our situs rules, income from the sale of personal property shall be treated as income from within the Philippines if the personal property is sold in the Philippines,<sup>114</sup> while compensation for services shall be treated as income from sources within the Philippines if the service is “performed in the Philippines.”<sup>115</sup>

In *P.F. Collier, Inc. (Philippine Branch) v. Commissioner of Internal Revenue*,<sup>116</sup> the Court of Tax Appeals held “the situs of sale of personal property for taxation purposes is the place where the sale is consummated and perfected.”<sup>117</sup> This case involved the sale of encyclopedia by P.F. Collier, U.S.A., a non-resident foreign corporation, to independent local distributors in the Philippines where the local distributors placed their specific orders to

---

111. NAT'L INTERNAL REVENUE CODE OF 1997, § 23 (B), (D), & (F).

112. *Id.* § 23 (A) & (E).

113. *Id.* § 42 (A) (3), (5), & (6).

114. *Id.* § 42 (A) (6) & (E).

115. *Id.* § 42 (A) (3).

116. *P.F. Collier, Inc. (Philippine Branch) v. Commissioner of Internal Revenue*, CTA Case No. 4355, Nov. 9, 1995, available at <http://cta.judiciary.gov.ph/home/download/abocdb142afb165c53e1848b68a63f91> (last accessed Jan. 8, 2021).

117. *Id.* at 1430.

the non-resident foreign corporation.<sup>118</sup> In turn, P.F. Collier, U.S.A. had the products shipped from the United States (U.S.) to the buyers in the Philippines.<sup>119</sup> The income from sales made by P.F. Collier, U.S.A., was deemed sourced outside the Philippines because “when the local distributors places and/or sent their specific orders to P.F. Collier, U.S. they already knew the price of Collier’s encyclopedia or books. Such orders were shipped by the vendor in the U.S. direct to the different vendees in the Philippines.”<sup>120</sup>

In BIR Ruling No. DA-512-04,<sup>121</sup> the BIR, citing *P.F. Collier, Inc.*, expressed the view that “[a] contract of sale is perfected at the moment there is a meeting of the minds upon the thing which is the object of the contract and the price and is consummated upon delivery of the object of the contract.”<sup>122</sup> This ruling involved the sale of products by a non-resident foreign corporation to a Philippine-based distributor.<sup>123</sup> The Philippine-based distributor will purchase products to supplier by sending purchase orders which will be subject to acceptance by supplier.<sup>124</sup> The confirmed orders were to be delivered by the supplier at the port of the country where the products are stored (e.g., Hongkong, Singapore, or Vietnam).<sup>125</sup> The BIR opined that the income earned by the supplier from the sale of the products is not sourced within the Philippines “considering that the perfection of the contract of sale and the delivery of [p]roducts will occur outside of the Philippines.”<sup>126</sup>

The foregoing supports the view that the income from sale of goods through the internet involving offshore sellers where the perfection and consummation of the contract is done outside the Philippines is not sourced within the Philippines, hence not subject to Philippine income tax.

With respect to sale of services online, the conclusion may be different. In the landmark case of *Commissioner of Internal Revenue v. British Overseas*

---

118. *Id.* at 1427.

119. *Id.* at 1431.

120. *Id.*

121. Bureau of Internal Revenue, Ruling No. DA-512-04 [BIR Ruling No. DA-512-04] (Sept. 30, 2004).

122. *Id.*

123. *Id.*

124. *Id.*

125. *Id.*

126. *Id.*

*Airways Corp.*,<sup>127</sup> the Supreme Court held that the “test of taxability is the ‘source’[ ] and the source of an income is that activity ... which produced the income.”<sup>128</sup> In *Alexander Howden & Co., Ltd. v. Collector of Internal Revenue*,<sup>129</sup> the Supreme Court explained that

‘income’ refers to the flow of wealth. Such flow ... proceeded from the Philippines. Such income enjoyed the protection of the Philippine Government. As wealth flowing from within the taxing jurisdiction of the Philippines and in consideration for protection accorded it by the Philippines, said income should properly share the burden of maintaining the government.<sup>130</sup>

In *Aces Philippines Cellular Satellite Corp. v. Commissioner of Internal Revenue*,<sup>131</sup> when confronted with determining whether payments for satellite air transmission through the use of Garuda Satellite (located in outer space) and Network Control Center (located in Indonesia) received by a non-resident foreign corporation are from sources within the Philippines,<sup>132</sup> the Court of Tax Appeals held that

[t]he satellite air time fees are considered as income from sources within the Philippines. The services for satellite [airtime] fees do not only compound with use of the Garuda Satellite (located in outer space) and the Network Control Center (located in Indonesia), but also require that satellite communication time be available and delivered in the Philippines. There is a continuous and very real connection starting from the Philippines (that is the agreement to sell satellite communications time for the ACES System in the Philippines), Garuda Satellite (located in outer space), the Network Control Center (located in Indonesia) and again the Philippines, through petitioner’s gateway facilities.

---

127. *Commissioner of Internal Revenue v. British Overseas Airways Corporation*, G.R. No. L-65773-74, 149 SCRA 395 (1987).

128. *British Overseas Airways Corp.*, 149 SCRA at 408 (citing *Alexander Howden & Co., Ltd.*, 13 SCRA at 604).

129. *Alexander Howden & Co., Ltd. v. Collector of Internal Revenue*, G.R. No. L-19392, 13 SCRA 601 (1965).

130. *Id.* at 605 (citing *Madrigal*, 38 Phil. at 418).

131. *Aces Philippines Cellular Satellite Corp. v. Commissioner of Internal Revenue*, CTA EB Case No. 1242, June 8, 2016, available at <http://cta.judiciary.gov.ph/home/download/1dfdc1fb84fbe1857118a017ead720do> (last accessed Jan. 8, 2021).

132. *Id.* at 11.

...

‘Income’ in our income tax law refers to the flow of wealth. [ACES International Limited’s] contract with petitioner extended its activities within the Philippine boundaries. It arises from the activity and services that produces the income within the Philippines. *The satellite [airtime] fees are income from sources within the Philippines. Thus, it enjoyed the protection of the government and should be controlled by the government. As wealth flowing from within the taxing jurisdiction of the Philippines, said income should properly share the burden of maintaining the government.* Accordingly, the jurisdiction of the Philippine government to tax must be upheld.<sup>133</sup>

In BIR Ruling No. 672-19,<sup>134</sup> the BIR stated that software distribution through online sale and CD boxes sale in the Philippines are deemed services being performed in the Philippines and are taxable here.<sup>135</sup> This was modified by the Department of Finance, which stated that the income payments should be classified as royalties and subject to income tax under the Philippines-Singapore Tax Treaty.<sup>136</sup>

*b. VAT on Online Shopping*

Under Section 105 of the 1997 NIRC, “[a]ny person who, in the course of trade or business, sells, barter, exchanges, leases goods or properties, renders services, and any person who imports goods shall be subject to the value-added tax ... .”<sup>137</sup>

The term “sells” is not defined in the 1997 NIRC. Under the Civil Code, a sale is defined as a contract where “one of the contracting parties obligates himself to transfer the ownership of and to deliver a determinate thing, and the other to pay therefor a price certain in money or its equivalent.”<sup>138</sup> It is

---

133. *Id.* at 12 & 15 (citing *Alexander Howden & Co., Ltd.*, 13 SCRA at 604) (emphasis supplied).

134. Bureau of Internal Revenue, Ruling No. 672-19 [BIR Ruling No. 672-19] (Oct. 30, 2019).

135. *Id.* at 4.

136. Department of Finance, Request for Review of Bureau of Internal Revenue Ruling No. 0672-2019, Opinion No. 10-2020, at 4 (Sept. 8, 2020).

137. NAT’L INTERNAL REVENUE CODE OF 1997, § 105.

138. CIVIL CODE, art. 1458.

also ordinarily understood as “to give up (property) to another for something of value (such as money).”<sup>139</sup>

The term “goods or properties” is defined in the 1997 NIRC as “all tangible and intangible objects which are capable of pecuniary estimation,”<sup>140</sup> while the phrase “sale or exchange services” refers to the “performance of all kinds of services in the Philippines for others for a fee, remuneration[,] or consideration.”<sup>141</sup>

In statutory construction, “[a] word of general significance in a statute is to be taken in its ordinary and comprehensive sense, unless it is shown that the word is intended to be given a different or restricted meaning.”<sup>142</sup> It appears that the term “sells” in Section 105 of the NIRC can be characterized as a word of general significance. This can be inferred from Section 105 itself when it only provided a meaning for the phrase “in the course of trade or business” and left other words without any restrictive definition.<sup>143</sup> There is also no indication in Section 105 that a different or restricted meaning of the term “sells” is being intended.<sup>144</sup> Therefore, the fact that a sale of goods or services was made online may be included in the ambit of VAT if the law is to be taken in its ordinary and comprehensive sense. The goods or properties which may either be “tangible or intangible” also appears broad enough to include sales of digital products which are intangible.<sup>145</sup> Furthermore, the term “sale or exchange of services” requires only that the service be performed for “a fee, remuneration, or consideration.”<sup>146</sup> The Court of Tax Appeals has held

---

139. Merriam-Webster, Definition of sell, available at <https://www.merriam-webster.com/dictionary/sell> (last accessed Jan. 8, 2021) [<https://perma.cc/PF7U-2AHZ>].

140. NAT'L INTERNAL REVENUE CODE OF 1997, § 106 (A) (1).

141. *Id.* § 108 (A).

142. RUBEN E. AGPALO, STATUTORY CONSTRUCTION 276 (6th ed. 2009) (citing *Calder & Co. v. U.S.*, 8 Phil. 334, 337 (1907); *Malicse v. Collector of Internal Revenue*, 99 Phil. 596, 599 (1956); *People v. Chaves*, G.R. No. L-19521, 12 SCRA 232, 234 (1964); & *Phil. Acetylene Co., Inc. v. Central Bank of the Philippines*, G.R. No. L-17097, 12 SCRA 38, 41-42 (1964)).

143. NAT'L INTERNAL REVENUE CODE OF 1997, § 105.

144. *Id.*

145. *See id.* § 106 (A) (1).

146. NAT'L INTERNAL REVENUE CODE OF 1997, § 108 (A).

that “the term ‘service’ is ordinarily defined as ‘help’ or ‘benefit.’”<sup>147</sup> The term “service” is ordinarily understood as “work performed by one that serves.”<sup>148</sup> Thus, as currently worded, these terms appear to be broad enough to cover digital products and services sold through the internet.

Therefore, assuming that the seller’s gross sales or receipts exceeds ₱3,000,000,<sup>149</sup> the onshore seller may be held liable for VAT because the sale of goods or services is within the Philippines unless the transaction is exempt under Section 109 of the 1997 NIRC.<sup>150</sup>

Liability for VAT may fall on a different person when an offshore seller of goods is involved. Under Section 105 of the 1997 NIRC, “any person who imports goods shall be [liable for VAT].”<sup>151</sup> In turn, under Section 107, the VAT shall be paid by the importer before the release of the goods.<sup>152</sup> Thus, in online shopping involving the importation of goods sold by an offshore seller, the VAT liability could be imposed on the importer of the goods.

## 2. Online Intermediary Service

As defined under RMC No. 55-2013, an online intermediary service “is a third party that offers intermediation services between two trading parties. The intermediary acts as a conduit for goods or services offered by a supplier to a consumer and receives commission therefor.”<sup>153</sup> There are four taxable activities typically involved in an online intermediary service transaction, namely: (a) the sale of goods or services between the seller and the buyer, (b) the service provided by the online intermediary service provider, (c) the

---

147. *Waterfront Philippines, Inc. v. Commissioner of Internal Revenue*, CTA Case No. 8024, Dec. 4, 2014, at 15 *available at* <http://cta.judiciary.gov.ph/home/download/4247d8eb2360e8b0503c7b18076d75> (last accessed Jan. 8, 2021).

148. Merriam-Webster, Definition of service, *available at* <https://www.merriam-webster.com/dictionary/service> (last accessed Jan. 8, 2021) [<https://perma.cc/VH88-5YPA>].

149. NAT’L INTERNAL REVENUE CODE OF 1997, § 236 (G) (1). Under Section 236 (H) of the 1997 NIRC, if the seller voluntarily registers under the VAT System, even if the gross sales or receipts do not exceed ₱3,000,000.00, the seller is liable for VAT. *Id.* § 236 (H).

150. *Id.* § 109.

151. *Id.* § 105.

152. *Id.* § 107 (A).

153. RMC No. 55-2013, at 2.

service provided by the payment gateway, and (d) the service performed by a logistics provider.<sup>154</sup>

The tax liability of the seller and buyer under the current tax regime as discussed above should also be applicable even though the sale is transacted through the aid of online intermediary service provider. The additional transaction involved is the one between the seller and the online intermediary. Under RMC No. 55-2013, “the relationship between the intermediary and the merchant (seller) shall be that of a principal-agent relationship which shall be governed by their agreement ... .”<sup>155</sup>

Under this set-up, an online intermediary undertakes a sale of service to the merchant in consideration of a service fee, usually in the form of a commission.<sup>156</sup> An online intermediary may be held liable for income tax for the taxable income realized from its conduct of trade or business. An online intermediary may either be physically onshore or offshore. To determine the situs of the income generated, the rules for sale of services involving online shopping discussed above may also be applied to the sale of service of an online intermediary service provider. Although it acts as a conduit between the seller and the buyer, the activity which produces the income may also be said to be within the Philippines because the seller pays for the online intermediary’s service of connecting it to buyers who may access the platform in the Philippines. Likewise, an online intermediary may also be liable for VAT for the sale its sale of service in the Philippines.

### 3. Online Advertisement/Classified Ads

Under RMC No. 55-2013, an online advertisement “is a form of promotion that uses the internet to deliver marketing messages to attract customers.”<sup>157</sup> There is an ad provider and a consumer which avails of its services. In an online advertisement transaction, the taxable activities would be: (a) the service provided by the ad provider to the consumer, and possibly (b) the service provided by a payment gateway.<sup>158</sup>

Like online shopping and online intermediary services, the income generated by an online advertisement provider is derived from the conduct of

---

154. *See id.* at 4-6.

155. RMC No. 55-2013, at 2.

156. *See id.*

157. RMC No. 55-2013, at 2.

158. *See id.* at 6-7.



its trade or business. As mentioned, compensation for services shall be treated as sourced within the Philippines when the service is performed in the Philippines.<sup>159</sup> “The important factor which determines the source of income of personal services is not the residence of the payor, or the place where the contract for service is entered into, or the place of payment, but the place where the services were actually rendered.”<sup>160</sup>

In *Marsman and Co., Inc. v. Commissioner of Internal Revenue*,<sup>161</sup> when confronted with resolving whether advertising fees received from ad placements made in the Philippines by Philippine advertisers to a non-resident foreign corporation are income within the Philippines, the Court of Tax Appeals held that the “advertising payments made by Philippine advertisers to petitioner are subject to the withholding tax, as these incomes are considered earned in the Philippines.”<sup>162</sup> In reaching this conclusion, the Court of Tax Appeals applied the principle laid down in *Commissioner of Internal Revenue v. British Overseas Airways Corp.*,<sup>163</sup> which looks at the activity which produces the income,<sup>164</sup> in determining the situs of income which in this case is the ad placements made in the Philippines by Philippine advertisers.

BIR Ruling No. 124-18<sup>165</sup> presented a different situation, where a domestic corporation engaged the services of a non-resident corporation to promote and market the products of that domestic corporation to its clients in Samoa and other foreign countries.<sup>166</sup> The BIR opined that the promotion and marketing services of the products performed by a non-resident foreign

---

159. NAT’L INTERNAL REVENUE CODE OF 1997, § 42 (A) (3).

160. *Commissioner of Internal Revenue v. Baier-Nickel*, G.R. No. 153793, 500 SCRA 87, 96 (2006) (citing JACOB MERTENS, *THE LAW OF FEDERAL INCOME TAXATION* 45C-32 (1996)).

161. *Marsman and Co., Inc. v. Commissioner of Internal Revenue*, CTA Case No. 5940, July 5, 2002, available at <http://cta.judiciary.gov.ph/home/download/d3dddafa3c8d8ee49e40c6ccc80118cb3> (last accessed Jan. 8, 2021).

162. *Id.* at 14-15.

163. *Commissioner of Internal Revenue v. British Overseas Airways Corporation*, G.R. No. L-65773-74, 149 SCRA 395 (1987).

164. *British Overseas Airways Corp.*, 149 SCRA at 408 (citing *Alexander Howden & Co., Ltd.*, 13 SCRA at 604).

165. Bureau of Internal Revenue, Ruling No. 124-2018 [BIR Ruling No. 124-2018] (Feb. 2, 2018).

166. *Id.* at 1.

corporation outside the Philippines is treated as services performed outside the Philippines.<sup>167</sup>

#### 4. Online Auction

Online auctions are “conducted through the internet via an online service provider that specifically hosts such auctions.”<sup>168</sup> An online auction typically involves the following transactions: (a) the sale of goods or services between the auction seller and the buyer-consumer, (b) the service provided by the online auction host, (c) the service provided by the payment gateway, and (d) the service performed by a logistics provider.<sup>169</sup>

The income tax and VAT implications for the transaction between the seller and the buyer in sales transacted through online auction are similar to the seller and buyer in online shopping or online retailing for sale of services.

The online webstore (or the auction host) may also obtain income from a buyer’s payment for vouchers, coupons, or bid packs<sup>170</sup> as fees for the right to participate in the bidding.<sup>171</sup> Following *Commissioner of Internal Revenue v. British Overseas Airways Corp.*,<sup>172</sup> if the activity which produced the income is the “right to bid” which is to be exercised within the Philippines: (a) the situs of those fees may be said to be within the Philippines for income tax purposes, and (b) the service is being performed in the Philippines for VAT purposes.

#### 5. Payment Gateways and Logistics Providers

In many online transactions, apart from the sellers, buyers, and intermediaries, payment gateways and logistics providers are also involved.<sup>173</sup>

##### *a. Payment Gateways*

RMC No. 55-2013 defines payment gateways as “banks or other organizations and third-party settlement organizations that has contractual obligation to

---

167. *Id.* at 2.

168. RMC No. 55-2013, at 2.

169. *Id.* at 7-8.

170. *Id.* at 7.

171. *Id.*

172. See *British Overseas Airways Corp.*, 149 SCRA at 408 (citing *Alexander Howden & Co., Ltd.*, 13 SCRA at 604).

173. See RMC No. 55-2013, at 3-6.

make payment to participating payees in the settlement of the transactions. These include, but are not limited to, credit card companies, banks, financial institution, and bill paying services.”<sup>174</sup>

Payment gateways essentially provide services. The income produced from the sale of services (i.e., the commission paid by the sellers) may give rise to a potential income tax liability. Like sellers, there can be onshore or offshore payment gateways and the liability for income tax or VAT may be different. For example, in BIR Ruling DA-(C-148) 406-09,<sup>175</sup> the BIR was asked to render an opinion on whether —

[PAY-ON AG], as a non-resident foreign corporation performing online payment processing services outside of the Philippines for customers located inside as well as outside of the Philippines, is not subject to Philippine taxation (income tax, withholding tax, and value added tax) on fees collected in the Philippines for customers located in the Philippines for such services performed outside of the Philippines[.]<sup>176</sup>

The BIR opined that “[PAY-ON AG] is not subject to Philippine taxes on fees collected in the Philippines for customers located in the Philippines for such services performed outside of the Philippines.”<sup>177</sup> Among the circumstances the BIR took into consideration are that “the actual service rendered is the online payment processing[.]”<sup>178</sup> and that the services are “hosted and performed outside the Philippines.”<sup>179</sup>

*b. Logistics Providers*

Logistic service providers are also typically involved in online business transactions.<sup>180</sup> They obtain income from the sale of services (e.g., for delivering goods ordered by buyers). Thus, the general principles on income tax and VAT liability for sale of services discussed above may be applied to logistics services involved in online business transactions.

---

174. RMC No. 55-2013, at 4.

175. Bureau of Internal Revenue, Ruling No. DA-(C-148) 406-09 [BIR Ruling No. DA-(C-148) 406-09] (July 24, 2009).

176. *Id.*

177. *Id.*

178. *Id.*

179. *Id.*

180. *See* RMC No. 55-2013, at 3-6.

Logistics providers may also be performing services within or without the Philippines. As far as income tax is concerned, an onshore logistics provider is subject to income tax for its taxable income earned within and without the Philippines, while an offshore logistics provider (e.g., foreign vessels or planes carrying goods from a foreign country to the Philippines) is only subject to income tax for income derived within the Philippines. Under Section 42 of the 1997 NIRC, compensation for labor or personal services performed in the Philippines shall be treated as gross income from source within the Philippines.<sup>181</sup> In *Commissioner of Internal Revenue v. British Overseas Airways Corp.*,<sup>182</sup> the Supreme Court, in resolving the argument of respondent that the test of situs for international transportation services is the place where the services are rendered, held that “[t]he absence of flight operations to and from the Philippines is not determinative of the source of income or the situs of income taxation[.]”<sup>183</sup> and “even if the BOAC tickets sold covered the ‘transport of passengers and cargo to and from foreign cities’, it cannot alter the fact that income from the sale of tickets was derived from the Philippines.”<sup>184</sup>

With respect to VAT, Section 108 (A) of the NIRC in defining “sale or exchange of services” includes

transportation contractors on their transport of goods or cargoes, including persons who transport goods or cargoes for hire and other domestic common carriers by land relative to their transport of goods or cargoes; common carriers by air and sea relative to their transport of passengers, goods or cargoes from one place in the Philippines to another place in the Philippines[.]<sup>185</sup>

Thus, if the delivery service is performed from one place in the Philippines to another place in the Philippines, the logistics provider would be subject to VAT.

---

181. NAT'L INTERNAL REVENUE CODE OF 1997, § 42 (A) (3).

182. *Commissioner of Internal Revenue v. British Overseas Airways Corporation*, G.R. No. L-65773-74, 149 SCRA 395 (1987).

183. *British Overseas Airways Corp.*, 149 SCRA at 408.

184. *Id.* at 409.

185. NAT'L INTERNAL REVENUE CODE OF 1997, § 108 (A).

## VI. TAX REGIMES IN OTHER JURISDICTIONS

The question as to how tax income is generated and capturing the value in online business transactions is a question not exclusive to the Philippines. In a 2015 Report by the Organisation for Economic Co-operation and Development (OECD), it was noted that the spread of digital economy raises fundamental questions as to how enterprises in the digital economy add value and make their profits, and how the digital economy relates to the concepts of source and residence or the characterization of income for tax purposes.<sup>186</sup> There seems to be a growing consensus among countries on the need to respond the challenges posed by the digital economy.<sup>187</sup>

This Chapter looks at the models adopted by other countries to tax the digital economy. This Chapter is divided into two Parts. The first Part looks at the legal framework of other countries — that is, whether they apply their general tax laws or have special rules for taxing their digital economy. The second Part looks at enforcement, which essentially revolves around withholding of taxes.

*A. Basic Legal Framework*

## 1. Countries Applying General Taxation Rules to Digital Economy

A general survey of the e-commerce tax regimes in 90 other jurisdictions shows that 42 countries appear to apply their general laws on taxation in respect of online transactions.<sup>188</sup> In other words, the regular rules on income and VAT (or their equivalent) are also applied to e-commerce transactions.

---

186. ORGANISATION FOR ECONOMIC CO-OPERATION AND DEVELOPMENT, ADDRESSING THE TAX CHALLENGES OF THE DIGITAL ECONOMY, ACTION 1 - 2015 FINAL REPORT 16 (2015).

187. *Id.*

188. Angola, Armenia, Aruba, Austria, Bahamas, Barbados, BES Islands, Bolivia, Botswana, Brazil, Canada, Chad, Congo, Dominican Republic, Ecuador, Egypt, El Salvador, Equatorial Guinea, Eswatini, Georgia, Guatemala, Guinea, Honduras, Kazakhstan, Lebanon, Malawi, Maldives, Mauritius, Mongolia, Myanmar, Namibia, Nicaragua, Nigeria, Panama, Rwanda, Saint Lucia, South Sudan, Suriname, Tunisia, Trinidad and Tobago, Venezuela, and Romania.

## 2. Countries with Special Tax Rules for Digital Economy

Out of the 90 tax jurisdictions surveyed, 48 appear to have established rules specifically dealing with e-commerce transactions.<sup>189</sup> The special tax rules in these jurisdictions range from regulating only direct taxes (e.g., income tax) or indirect taxes (e.g., VAT, GST, or sales tax), or both.

### *a. Income*

In an apparent response to the situs issues brought about by e-commerce transactions, some countries have introduced the concept of significant economic presence (SEP) as a new nexus test.<sup>190</sup> India, Italy, and Nigeria are some of the countries which included SEP in their tax rules.<sup>191</sup>

In India, the Income Tax Act introduced the SEP in their income tax laws to expand the scope of a business connection that results in the taxation of business income of nonresidents in India targeted to tax business models in the digital economy.<sup>192</sup> Italy's version which first appeared in their 2018 Budget Law defines SEP as “[a] continuous and significant economic presence of a foreign company in Italy, regardless of whether it has a substantial Italian physical presence[.]”<sup>193</sup> In Nigeria, taxable income derived by foreign companies includes income from digital services if such foreign companies have significant economic presence in Nigeria.<sup>194</sup>

---

189. Albania, Algeria, Argentina, Australia, Austria, Azerbaijan, Bahrain, Bangladesh, Belarus, Belgium, Bulgaria, Cameroon, Chile, China, Colombia, Costa Rica, Estonia, Germany, Ghana, India, Indonesia, Israel, Italy, Japan, Jersey Channel Islands, Kenya, Korea, Kosovo, Malaysia, Mexico, Moldova, Netherlands, New Zealand, Norway, Pakistan, Paraguay, Quebec, Russia, Saudi Arabia, Singapore, South Africa, Switzerland, Taiwan, Turkey, Turkey, Uzbekistan, Vietnam, and Zambia.

190. ORGANISATION FOR ECONOMIC CO-OPERATION AND DEVELOPMENT, *supra* note 186, at 107.

191. EY, *Worldwide Corporate Tax Guide 2020*, at 736, 841, & 1221, available at [https://assets.ey.com/content/dam/ey-sites/ey-com/en\\_gl/topics/tax/tax-pdfs/ey-wctg-web-final-11-december-2020.pdf?download](https://assets.ey.com/content/dam/ey-sites/ey-com/en_gl/topics/tax/tax-pdfs/ey-wctg-web-final-11-december-2020.pdf?download) (last accessed Jan. 8, 2021) [<https://perma.cc/B5HJ-EYD5>].

192. *Id.* at 736.

193. *Id.* at 841.

194. *Id.* at 1221.

*b. Indirect Tax*

Under the destination principle, goods and services are taxed in the country where these are consumed.<sup>195</sup> Some countries have introduced standards to determine where digital transactions are consumed such as effective use, virtual presence, and domicile or residence of the consumer.

*i. Effective Use*

In Argentina, digital services received by Argentine individuals are subject to VAT in Argentina when rendered by foreign parties where the effective use of the services or exploitation is conducted in Argentina.<sup>196</sup> Argentine law establishes presumptions of effective use when the consumer is located in Argentina such that the IP address of the device used by the customer or SIM card country code is in Argentina, the billing address of the local client; the bank account used for the payment, the billing address of the customer that the bank has or the financial institution issuing the credit or debit card with which the payment is made.<sup>197</sup>

*ii. Virtual Presence*

Though not entirely applicable throughout Pakistan, the provinces of Sindh and Punjab have amended their sales tax laws which looks at the virtual presence of a digital service provider.<sup>198</sup> In this amendment, a person carrying on economic activity through a virtual presence or a website or a web portal or through any other form of e-commerce is treated as having a place of business in Sindh and Punjab.<sup>199</sup>

---

195. *Atlas Consolidated Mining and Development Corp.*, 524 SCRA at 103 (citing *Seagate Technology (Philippines)*, 451 SCRA at 144 n. 53).

196. EY, *Worldwide VAT, GST and Sales Tax Guide*, at 35, available at [https://assets.ey.com/content/dam/ey-sites/ey-com/en\\_gl/topics/tax/tax-pdfs/ey-2020-vat-guide-19may-2020.pdf?download](https://assets.ey.com/content/dam/ey-sites/ey-com/en_gl/topics/tax/tax-pdfs/ey-2020-vat-guide-19may-2020.pdf?download) (last accessed Jan. 8, 2021) [<https://perma.cc/S7L8-QN9C>].

197. Augusto Nicolás Mancinelli, *Argentina Introduces VAT on Digital Services*, available at <https://www.dlapiper.com/en/us/insights/publications/2018/09/argentina-introduces-vat-on-digital-services/> (last accessed Jan. 8, 2021) [<https://perma.cc/QB9M-KXH4>].

198. EY, *supra* note 196, at 965.

199. *Id.*

### iii. Domicile of the Consumer

Twenty-one of the jurisdictions surveyed have set rules to determine where goods or services are consumed in the context of e-commerce transactions. For instance, in Albania and Australia, the place of supply of cross-border digital services is the place where the consumer is established, has permanent address, or usual residence.<sup>200</sup> In Azerbaijan, the consumption is destined where the consumer is located.<sup>201</sup> In Bahrain, the place where the contract with the consumer is executed or where the services are paid is not considered, but the place of use and enjoyment is the place where the customer actually resides and enjoys the service.<sup>202</sup>

### B. Enforcing Digital Tax

In terms of tax collection and administration, other jurisdictions have institutionalized mechanisms which attempt to capture the complex nature of digital transactions. Among these include self-assessment by consumers, mandatory registration for persons engaged in online business transactions, and withholding taxes.

#### 1. Registration

To aid in the collection and enforcement of an indirect tax, several jurisdictions have mandated registration of parties involved in online business transactions. Among these are Albania,<sup>203</sup> Bangladesh,<sup>204</sup> Belarus,<sup>205</sup> Chile,<sup>206</sup>

---

200. *Id.* at 5 & 61-62.

201. *Id.* at 90.

202. *Id.* at 108.

203. *Id.* at 6.

204. EY, *supra* note 196, at 124.

205. *Id.* at 141-42.

206. *Id.* at 253.



Ghana,<sup>207</sup> Indonesia,<sup>208</sup> Italy,<sup>209</sup> Mexico,<sup>210</sup> Quebec,<sup>211</sup> Taiwan,<sup>212</sup> and Vietnam.<sup>213</sup>

Special registration systems for foreign VAT taxpayers are also set in place in Norway<sup>214</sup> and Singapore through an overseas vendor registration (OVR) regime,<sup>215</sup> and in Turkey through a special VAT registration for electronic service providers.<sup>216</sup>

In Mexico, noncompliance with obligations to register, appointment of a legal representative and tax domiciles, or failure to file returns in specified instances allow the tax authorities to block the internet webpage.<sup>217</sup>

## 2. Withholding or Collection

Probably recognizing the difficulty in enforcing mandatory registration especially in the context of non-resident suppliers or digital platforms and the difficulty of policing the internet, other countries have also devised means to withhold taxes. The primary difference lies with the person constituted as withholding agent by the taxing authority. In some countries, it is the e-commerce platform which is constituted as withholding agent. In other countries, it is the financial intermediary (e.g., banks or credit card providers) which is constituted as withholding agent.

### *a. Platform*

In Australia, it is the operator of an electronic distribution platform which may be subject to responsibility of paying the GST.<sup>218</sup> In India, an electronic commerce operator, in certain instances, is mandated to collect an amount not

---

207. *Id.* at 502.

208. *Id.* at 592-93.

209. *Id.* at 641.

210. EY, *supra* note 196, at 850.

211. *Id.* at 230.

212. *Id.* at 1251-252.

213. *Id.* at 1406.

214. *Id.* at 951.

215. *Id.* at 1140.

216. EY, *supra* note 196, at 1296.

217. *Id.* at 856.

218. *Id.* at 62.

exceeding one percent of the net value of the taxable supplied made through it by other suppliers where the consideration with respect to such supplies is to be collected by the operator.<sup>219</sup> The amount collected is called tax collected at source (TCS).<sup>220</sup> In Cameroon, sales of goods through foreign or local e-commerce platforms shall trigger an obligation on the part of the e-commerce platform to register for VAT and calculate, declare, and pay VAT on sales of goods or services through their platforms.<sup>221</sup> Mexico also recently enacted its Tax Reform Law for the year 2020 which mandates non-Mexican residents acting as intermediaries to withhold from individuals 50% of the VAT collected and register as withholding agent.<sup>222</sup> In China, there are also instances where corporations specializing in e-commerce transactions can be withholding agents for VAT.<sup>223</sup> In Norway, if the electronic services are supplied through a mediator or an online marketplace or platform, the supplier is considered to sell the services to the intermediary and the intermediary, in turn, is deemed to have transferred the services to the buyer.<sup>224</sup>

In South Korea, when “a foreign corporation provides electronic services through an online marketplace or platform, that marketplace or platform company is considered to provide electronic services in Korea.”<sup>225</sup> In this situation, it is the platform or marketplace who bears the burden of accounting for the VAT on the supplies made.<sup>226</sup> Likewise, “[s]uppliers who only supply remote services or low-value goods to New Zealand customers through an ‘electronic marketplace’ operated by a nonresident person will generally not be required to register for GST in respect of the supplies made through the

---

219. Central Goods and Services Tax Act, 2017, Act No. 12 of 2017, § 52 (1) (2017) (India).

220. Cleartax, Tax Collected At Source (TCS) Under Goods and Services Tax, *available at* <https://cleartax.in/s/tcs-under-goods-and-services-tax> (last accessed Jan. 8, 2021) [<https://perma.cc/H7WF-WJDW>].

221. Finance Law of the Republic of Cameroon for the 2020 Financial Year, Law No. 2019/023, § 149c (1) (2019) (Cameroon).

222. Ley Del Impuesto Sobre La Renta, DOF 09-12-2019, art. 18-J (2019) (Mex.).

223. Mazars, May 2019 - China Adopts E-commerce Law – Its Tax Implications, *available at* <http://www.mazars.cn/Home/Insights/Our-publications/Tax-publications/China-Tax-Newsletter/May-2019-China-Adopts-E-commerce-Law> (last accessed Jan. 8, 2021) [<https://perma.cc/78YE-3PAN>].

224. EY, *supra* note 196, at 951.

225. *Id.* at 709.

226. *Id.*

marketplace.”<sup>227</sup> It is the nonresident operator of the marketplace which is generally liable to register and return GST on behalf of its underlying suppliers.<sup>228</sup> In Saudi Arabia, the online intermediary is presumed to purchase the services from the nonresident supplier in certain cases where electronically-supplied services are supplied in Saudi Arabia through an online interface or portal acting as intermediary for a nonresident supplier.<sup>229</sup>

## VII. THE WAY FORWARD

Although existing tax laws permit the imposition of income tax and VAT on certain online transactions, there are still areas where having clear and simple rules would be helpful. For instance, the application of situs rules when applied to online business transactions and the proper characterization of digital products and services still leave room for interpretation under the current tax regime. With respect to VAT, it would also be ideal if the place where e-commerce transaction is performed is clarified.

This Section examines the pending bills in Congress which seek to amend the 1997 NIRC and introduce provisions dealing with digital transactions and the possible measures which may be employed to make our tax laws in synch with the times and advances in technology.

### A. *Income Tax*

H.B. No. 6765 proposes to impose withholding tax at source on network orchestrators.<sup>230</sup> Network orchestrators refer to “persons, typically aided by information technology, that ... create a network of accredited service providers and service consumers, and that act as intermediaries that facilitate the matching of a consumer’s service needs with a provider’s available services.”<sup>231</sup> Under the proposed amendment, “[w]hen taxable income and/or revenue is derived through membership in a network orchestrator system, the tax imposed under Section 24 (A) of [the 1997 NIRC] shall be withheld by the network orchestrator.”<sup>232</sup> The stated purpose is to ease the partners (or

---

227. *Id.* at 916.

228. *Id.*

229. *Id.* at 1114.

230. H.B. No. 6765, explan. n.

231. *Id.* § 3 (c).

232. *Id.* § 4.

service providers) of network orchestrators of the burden of having to pay their own taxes, and at the same time to encourage tax compliance.<sup>233</sup>

This proposal was omitted in the substitute bill, H.B. No. 7425 which seek to amend Sections 105, 108, 109, 110, 113, 114, and 236 (on VAT) of the 1997 NIRC.<sup>234</sup> H.B. No. 7425 also removed proposals in H.B. No. 6765 which seek to amend Section 57 (on income tax) of the 1997 NIRC.

### B. VAT

H.B. No. 7425, among others, proposes a new section specifically dealing with digital or electronic transactions and the definition of term “buyer” in the context of digital transactions, as follows —

Sec. 105-A. Persons Liable in Digital or Electronic Transactions. — The nonresident digital service provider is liable for assessing, collecting, and remitting the value-added tax on the transactions that go through its platform.

For this purpose, the term ‘digital service provider’ refers to a service provider of a digital service or good to a buyer, through operating an online platform for purposes of buying and selling of goods or services or by making transactions for the provision of digital services on behalf of any person: *Provided*, that the digital service provider may be:

- (1) A third party, such as a seller of goods or services who, through information-based technology or the internet sells multiple products for its own account, or one who acts as an intermediary between a supplier and buyer of goods and services, such as a merchandiser or retailer, who collects or receives payment for such goods and services from a buyer in behalf of the supplier and receives a commission thereon;
- (2) A platform provider for promotion that uses the internet to deliver marketing messages to attract buyers;
- (3) A host of online auction conducted through the internet, where the seller sells the product or service to the person who offers the highest price for it;
- (4) A supplier of digital services to a buyer in exchange for a regular subscription fee over the usage of the said product or service; and

---

233. *Id.* explan. n.

234. *See* H.B. No. 7425.

- (5) A supplier of goods or electronic and online services that can be delivered through an information technology infrastructure, such as the internet.

For this purpose, the term ‘buyer’ refers to any person who resides in the Philippines and who acquires taxable digital services in the Philippines from a digital service provider either for personal consumption, or for trade or business purposes. The term ‘digital service’ refers to any service that is delivered or subscribed over the internet or other electronic network and which cannot be obtained without the use of information technology and where the delivery of the service may be automated. Digital services shall include online licensing of software, updates, and add-ons, website filters and firewalls; mobile applications, video games, and online games; webcast and webinars; provision of digital content such as music, files, images, text and information; advertisement platform such as provision of online advertising space on intangible media platform; online platform such as electronic marketplaces or networks for the sale, display, and comparison of prices of trade products or services; search engine services; social networks; database and hosting such a website hosting, online data warehousing, file sharing and cloud storage services; internet-based telecommunication; online training such as provision of distance teaching, e-learning, online courses and webinars; online newspapers and journal description; and payment processing services.<sup>235</sup>

The stated purpose is to “[clarify] the imposition of VAT on electronic or online sale of services”<sup>236</sup> and to define the liability of digital service providers.<sup>237</sup> With the inclusion of a definition for the term “buyer,”<sup>238</sup> H.B. No 7425 appears to set a standard as to when a sale of goods or service is deemed within the Philippines.

The introduction of a statutory definition of “buyer” in digital or electronic transactions would help provide some clarity as to whether online business transactions are considered “within the Philippines.” Under the 1997 NIRC, it is essential that for a sale of goods or services to be subject to VAT the sale of goods or services must be within the Philippines.<sup>239</sup> The proposed provision, in a sense, provides a clearer standard for purposes of digital transactions. A “buyer” refers to “any person who resides in the Philippines and who acquires taxable digital services in the Philippines from a digital

---

235. H.B. No. 7425, § 2.

236. H. Comm. Rep. No. 426, at \*17.

237. *Id.*

238. H.B. No. 7425, § 2.

239. NAT’L INTERNAL REVENUE CODE OF 1997, §§ 106 (A) & 108 (A).

service provider either for personal consumption, or for trade or business purposes.”<sup>240</sup> Under this proposed definition, lingering questions of whether the sale of goods or services is made within the Philippines under the current tax regime may be avoided because it appears that one simply has to look at two things: one, whether the buyer is residing in the Philippines, and two, whether the buyer acquired the taxable digital services in the Philippines.

Having simple and clear standards for determining the place where digital services are performed would reduce the room for varying interpretations including, for example, BIR Ruling No. 009-05<sup>241</sup> where the BIR expressed the view that “[c]onsidering that the services that produce the income (i.e., registration and maintenance of [Philippine] domain names) are performed outside of the Philippines, it follows that the income derived from the performance of such services is *not* taxable in the Philippines.”<sup>242</sup>

The proposed definition seems to be similar to what has been adopted in other jurisdictions which have included in their VAT rules the consumer’s residence, domicile, or location for purposes of determining whether the sale of digital goods or services is subject to VAT.

### C. Tax Enforcement and Collection

H.B. No. 7425 proposes two tax enforcement provisions: *first*, it requires non-resident digital service providers to register for VAT under certain conditions;<sup>243</sup> *second*, it makes non-resident digital service providers liable for assessing, collecting, and remitting VAT on the transactions that go through its platform.<sup>244</sup> The evident purpose is to aid in the collection of VAT from persons who may not otherwise be within reach of our taxing authorities because they do not have physical presence in the Philippines. The proposal is notable because, even as the 1997 NIRC is broadly couched to include the imposition of VAT on sales of goods or services in the Philippines, tax enforcement could be difficult in digital or electronic transactions, especially where a seller is not residing in the Philippines. Philippine tax authorities may find it challenging to effectively collect taxes from a digital platform providing music streaming services in consideration of a subscription fee if it has no agent

---

240. H.B. No. 7425, § 2.

241. Bureau of Internal Revenue, Ruling No. 009-05 [BIR Ruling No. 009-05] (Aug. 2, 2005).

242. *Id.* (emphasis supplied).

243. H.B. No. 7425, § 8.

244. *Id.* § 2.

or representative here, or otherwise have no properties that may be subject to levy and attachment.

#### I. VAT Registration

H.B. No. 7425 seeks to make it mandatory for non-resident digital service providers to register for VAT,<sup>245</sup> as follows —

Sec. 236. Registration Requirements —

...

(G) Persons Required to Register for Value-Added Tax. —

...

(3) Any nonresident digital service provider who, in the course of trade or business, engages in the sale or exchange of digital services defined under this act, shall be liable to register for Valued-Added Tax if:

(a) The gross sales or receipts of such digital service business for the past [ ]12[ ] months before the date of filing of VAT return, other than those that are exempt under Section 109 (A) to (BB), have exceeded three million pesos (~~₱~~3,000,000); [o]r

(b) There are reasonable grounds to believe that the gross sales or receipts of the digital service business for the next [ ]12[ ] months from the date of filing of VAT return, other than those that are exempt under Section 109 (A) to (BB), will exceed three million pesos (~~₱~~3,000,000);

*Provided*, that the BIR shall establish a simplified automated registration system for nonresident digital service providers subject to the rules and regulations to be prescribed by the Secretary of Finance upon the recommendation of the Commissioner of Internal Revenue.<sup>246</sup>

H.B. No. 7425 seeks to ensure that VAT is enforced on persons otherwise not ordinarily within the reach of taxing authorities. Requiring VAT registration for non-resident foreign suppliers of digital services is similar to the VAT registration required in Albania, Bangladesh, Belarus, Chile, Ghana, Indonesia, Italy, Mexico, Quebec, Taiwan, Vietnam, Norway, Singapore, and Turkey.<sup>247</sup>

---

245. *Id.* § 8.

246. *Id.*

247. *See* EY, *supra* note 196.

## 2. Collecting Agents

In terms of tax collection, H.B. No. 6765 proposed to make the network orchestrator system or electronic commerce platforms as withholding agents responsible for deducting and withholding the VAT due from the seller,<sup>248</sup> while H.B. No. 7425 proposes to make non-resident digital service providers “liable for assessing, collecting, and remitting the [VAT] on the transactions that go through its platforms.”<sup>249</sup>

These proposed provisions are tax administration provisions which intend to facilitate tax collection and address the absence of a tax collection mechanism under the 1997 NIRC specifically dealing with multiple transactions concluded via the internet. The proposed amendment appears to be similar to what is being done in other jurisdictions like Australia, Cameroon, and India where e-commerce platforms may be constituted as collecting agents of the government for purposes of collecting VAT or its equivalent.<sup>250</sup>

A point to consider in shifting the administrative burden of collecting taxes to e-commerce platforms is the potential impact on transaction costs. Apart from withholding the tax due, withholding agents would also be responsible for submitting the appropriate returns and remitting the tax withheld. This may entail additional administrative costs (e.g., maintaining proper records of transactions, accounting services, and other costs associated with the processes of having to file returns and remit taxes) which may be passed on to the consumers in the form of higher fees or selling price of the goods or services. The other point to consider is whether the additional bureaucratic processes may be a barrier for new players in the e-commerce market or discourage the growth of start-up businesses.

A balancing of interests would have to be involved. On the one hand, the government has an interest to keep up with the pace (given that almost every conceivable transaction is being digitalized) and ensure that the proper and fair amount of taxes are effectively collected. With limited resources to monitor and ensure that each transaction concluded electronically is compliant with tax laws and regulations, it is to the government’s interest to align its tax collection strategy with the aim of minimizing enforcement costs and maximizing revenue returns. On the other hand, businesses have an interest to ensure that

---

248. H.B. No. 6765, § 7.

249. H.B. No. 7425, § 2.

250. See EY, *supra* note 196.



consumers will support their products and services by making these attractive not only with respect to quality, but also with respect to price.

While the proposed amendments to the 1997 NIRC are commendable as they seek to clarify tax laws to catch up with rapid technological advancements and aid in proper collection of taxes, the proposals may also have to hurdle public sentiments which have not been favorable mainly due to the adverse economic impact caused by the COVID-19 pandemic.<sup>251</sup> Additionally, the Philippine government would also have to be equipped with the appropriate information and communication technology facilities to ensure that it can effectively monitor tax compliance of e-commerce platforms. In the end, it is hoped that all of the legitimate interests and considerations are weighed and balanced properly, and the legislation which may be enacted would hopefully deliver the most benefit to the nation.

---

<sup>251</sup>Salaverria, *supra* note 13.