

## Tax Arbitrage in the Philippine Setting — Tax Evasion or Tax Avoidance?

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As a means of attempting to escape tax liabilities, tax advisers come up with myriad transactions which are entered for purposes of reducing taxes. One such transaction is tax arbitrage. Tax arbitrage refers to any investment which generates a profit because one part of the transaction is taxed differently from the other part. In the Philippine setting, many high income taxpayers resort to various forms of tax arbitrage available under the National Internal Revenue Code (NIRC), back-to-back loan agreements being the most risk-free.

This Note tackles to what extent a taxpayer may go in manufacturing interest deduction. The Author determines the propriety of deducting interest on borrowings to finance tax-favored investments when the transaction is entered into solely to reduce taxes by focusing on back-to-back loan agreements.

Part I of the Note explains the concept of tax arbitrage; Part II cites common arbitrage opportunities under the NIRC; Part III studies the legislative history of the Tax Code provisions on interest income and deductions to ascertain legislative intent; Part IV distinguishes tax avoidance and tax evasion; and Part V analyzes all possible arguments against tax arbitrage bearing in mind the well-settled rule that the taxpayer has the right to decrease or altogether avoid his taxes by means which the law permits.