REPUBLIC OF THE PHILIPPINES
DEPARTMENT OF FINANCE
BUREAU OF INTERNAL REVENUE
Quezon City

Sec. 34 (F), NIRC	
BIR Rulings No. 144-13	
OT - 0507 - 2020	

SEP 08 2020

Lock Law Office
No. 88, N. Jacinto Street
BF Classic Homes Village,
Parañaque City

Attention: **Atty. Roberto Belarmino M. Lock**

Gentlemen:

This refers to your letter dated November 8, 2019 requesting on behalf of your client, **Southbay Bulk Terminal Inc.,** ("SBTI") for confirmation of the proposed change in useful life of certain assets, for tax and financial accounting purposes, beginning January 1, 2020, pursuant to Section 34(F)(3) of the National Internal Revenue Code (NIRC) of 1997, as amended.

As represented, SBTI is a domestic corporation engaged in the business services of different kinds of chemicals and petroleum-chemicals for terminal and storage operations as well as consultancy thereon and other similar services of the same nature.

SBTI's fixed assets, particularly the Jetty facility and the Storage Tanks, were subjected to assessment by their Terminal Manager, Emerson R. Tesalona. He recommended to reduce the useful life of the subject assets in accordance with the following schedule:

Assets	Current Useful Life	Proposed Useful Life
1. Jetty Facility	30 years	15 years
2. Storage Tanks	20 years	15 years

The recommendation by Mr. Tesalona was predicated on several factors namely:

1. Impact of climate change on the coastal infrastructure;
2. Delayed periodic maintenance due to safety concerns; and
3. Issuance of an Annual Probationary Miscellaneous Lease from DENR limiting the duration of operation.

Mr. Tesalona's Assessment Report was approved by SBTI's Board of Directors which authorized the shortening of the estimated useful lives of the subject assets during its meeting held last July 23, 2019.

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In reply, please be informed that Section 34 (F)(1) of the NIRC provides that there shall be allowed as a depreciation deduction a reasonable allowance for the exhaustion, wear and tear (including reasonable allowance for obsolescence) of property used in the trade or business.

The term "reasonable allowance" shall include, but not limited to, an allowance computed in accordance with rules and regulations prescribed by the Secretary of Finance, upon recommendation of the Commissioner, under any of the following methods:

a. The straight-line method;
b. Declining-balance method, using a rate not exceeding twice the rate which would have been used had the annual allowance been computed under the method described in Subsection (F) (1);
c. The sum-of-the-years-digit method; and
d. Any other method which may be prescribed by the Secretary of Finance upon recommendation of the Commissioner. (Sec. 34 (F)(2), NIRC)

Corollarily, Section 34 (F) (3) of the NIRC, as amended, provides that —

"(3) Agreement as to Useful Life on which Depreciation Rate is Based. — Where under rules and regulations prescribed by the Secretary of Finance, upon recommendation of the Commissioner, the taxpayer and the Commissioner have entered into an agreement in writing specifically dealing with the useful life and rate of depreciation of any property, the rate so agreed upon shall be binding on both the taxpayer and the National Government in the absence of facts and circumstances not taken into consideration during the adoption of such agreement. The responsibility of establishing the existence of such facts and circumstances shall rest with the party initiating the modification. Any change in the agreed rate and useful life of the depreciable property as specified in the agreement shall not be effective for taxable years prior to the taxable year in which notice in writing by certified mail or registered mail is served by the party initiating such change to the other party to the agreement.

Provided, however, That where the taxpayer has adopted such useful life and depreciation rate for any depreciable asset and claimed the depreciation expenses as deduction from his gross income, without any written objection on the part of the Commissioner or his duly authorized representative, the aforesaid useful life and depreciation rate so adopted by the taxpayer for the aforesaid depreciable asset shall be considered binding for purposes of this Subsection."

Moreover, Section 105 of Revenue Regulations No. 2, otherwise known as the "Income Tax Regulations" reads —

"Section 105. Depreciation. — A reasonable allowance for the exhaustion, wear and tear, and obsolescence of property used in the trade or business may be deducted from gross income. For convenience, such an allowance will usually be referred to as depreciation, excluding from the term any idea of a mere reduction in market value not resulting from exhaustion, wear and tear, or obsolescence. The proper allowance for such depreciation of any property used in the trade or business is that amount which should be set aside for the taxable year in accordance with a reasonable consistent plan whereby the aggregate of the amount so set aside, plus the salvage value, will, at the end of the useful life of the property in business, equal the basis of the property. Due regard must also be given to expenditures for current upkeep."

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Furthermore, Section 109 of said Regulations No. 2 likewise reads —

> *"Section 109. Method of computing depreciation allowance. — The capital sum to be replaced should be charged off over the useful life of the property, either in equal instalment or in accordance with any other recognized trade practices, such as an apportionment of the capital sum over units of production. Whatever plan or method of apportionment is adopted must be reasonable and must have due regard to operating conditions during the taxable period. While the burden of proof must rest upon the taxpayer to sustain the deductions taken by him, such deductions must not be disallowed unless shown by clear and convincing evidence to be unreasonable. The reasonableness of any claim for depreciation shall be determined upon the conditions known to exist at the end of the period for which the return is made. If it develops that the useful life of the property will be longer or shorter than useful life as originally estimated under all the then known facts, the portion of the cost of other basis of the property not already provided for through depreciation allowances should be spread over the remaining useful life of the property as re-estimated in the light of the subsequent facts, and depreciation deductions taken accordingly."*

Based on the foregoing, the taxpayer and the Commissioner may agree on the estimated useful life and rate of depreciation of any property. The rate so agreed upon shall be binding on both the taxpayer and the BIR. However, if it develops that the useful life of the property originally estimated under previous factual conditions is no longer reasonable, the law allows the taxpayer to lengthen or shorten the useful life of the property in the light of prevailing factual considerations.

It has been ruled that the remaining estimated useful life of the assets is determined as that period of time expressed in years that an asset is expected to perform, in a satisfactory manner, the function for which it was designed and built, assuming normal and reasonable maintenance. The estimates of remaining life for each item of property had been based, in a very large measure, upon the observed condition at the time of appraisal and condition of maintenance, and the consideration of normal rates of depreciation for the type of property.

In view of the foregoing, this Office hereby CONFIRMS the proposed change by SBTI in useful life of Subject Assets in claiming depreciation deduction, for both tax and financial accounting purposes, beginning January 1, 2020, provided, however, that any prior period adjustments shall be subject to deficiency income tax, interest and penalties, if warranted.

This ruling is being issued on the basis of the foregoing facts as represented. However, if upon investigation, it will be ascertained that the facts are different, then this ruling shall be considered null and void.

Very truly yours,

CAESAR R. DULAY
Commissioner of Internal Revenue

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