REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

Special Third Division

SPOUSES MICHAEL GAVIN RICHARD L. DE LOS REYES AND JENNIFER C. CO-DE LOS REYES,
Petitioners,

CTA Case No. 9305

-versus-

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

Members:
FABON-VICTORINO, *Acting Chairperson, and*
RINGPIS-LIBAN, *JJ.*

Promulgated:

FEB 2 1 2019
12:45 p.m.

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DECISION

RINGPIS-LIBAN, *J.*:

This is a claim for refund, via the instant Petition for Review[1], filed by Spouses Michael Gavin Richard L. De Los Reyes and Jennifer C. Co-De Los Reyes involving their alleged erroneously paid and illegally collected income tax in the aggregate amount of Two Million One Hundred Twenty-One Thousand Three Hundred Fifty-Nine Pesos (₱2,121,359.00) for the taxable year 2013.

THE FACTS

The petitioners, Spouses Michael Gavin Richard L. De Los Reyes and Jennifer C. Co-De Los Reyes, are Filipinos, of legal age, with address at 6 ADB Avenue, Mandaluyong City. Petitioners may be served with notices and other

[1] Docket (Vol. I), pp. 10-23.

processes of this Honorable Court through their counsel, Carag Zaballero Llamado & Abiera Law Offices, with office address at Suite 2602, 26th Floor, The Atlanta Centre, No. 31 Annapolis Street, Greenhills, San Juan City, Metro Manila.[2]

In the taxable year 2013, petitioners worked as staff members of the Asian Development Bank (ADB). Mr. Michael Gavin Richard L. De Los Reyes is a Treasury Specialist in the Treasury Department (Treasury Clients Solutions Unit)[3], while his spouse Jennifer C. Co-De Los Reyes is the Compensation and Benefits Officer of the Budget, Personnel, and Management Systems Department (HR Policy and Program Division)[4].

On the other hand, respondent is the duly appointed Commissioner of the Bureau of Internal Revenue (BIR), who is vested by law with authority to decide, approve and grant claims for refund or tax credit of erroneously or excessively paid taxes. He holds office at the BIR National Office Building, Agham Road, Diliman, Quezon City.

On April 12, 2013, the BIR issued Revenue Memorandum Circular (RMC) No. 31-2013[5], the pertinent provisions of which state:

> **"SECTION 2. TAX TREATMENT OF COMPENSATION INCOME**
>
> The tax treatment of Philippine nationals and alien individuals on compensation income received by them from foreign governments/embassies and missions and international organizations shall be as follows:
>
> x x x
>
> **(d) Those Employed by Organizations Covered by Separate International Agreements or Specific Provisions of Law –**
>
> **1. Asian Development Bank (ADB)**
>
> Section 45(b), Article XII of the **Agreement between the Asian Development Bank and the Government of the Republic of the**

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[2] Paragraph 1.1, Joint Stipulation of Facts and Issues (JSFI), *ibid*, p. 319.
[3] Exhibit "P-2".
[4] Exhibit "P-3".
[5] Subject: Guidelines on the Taxation of Compensation Income of Philippine Nationals and Alien Individuals Employed by Foreign Governments/Embassies/Diplomatic Missions and International Organizations Situated in the Philippines.

Philippines regarding the Headquarters of the Asian Development Bank provides:

'ARTICLE XII

x x x

Section 45

<u>Officers and staff of the Bank, including for the purposes of this Article experts and consultants performing missions for the Bank,</u> shall enjoy the following privileges and immunities:

x x x

(b) Exemption from taxation on or in respect of the salaries and emoluments paid by the Bank <u>subject to the power of the Government to tax its nationals;</u>' Underscoring supplied

From the above, only officers and staff of the ADB who are not Philippine nationals shall be exempt from Philippine income tax.

x x x

SECTION 3. FILING OF INCOME TAX RETURNS AND DECLARATION OF COMPENSATION INCOME. – Philippine nationals and alien individuals who were not granted tax exemption or immunities under duly recognized international agreements or local laws shall file their annual income tax returns on or before the 15th day of April each year using BIR Form No. 1700 or 1701, as may be applicable[6], declaring therein the amount of their respective compensation income for the preceding taxable year for services rendered or performed for such foreign government embassy/diplomatic mission, agency or international organization.

The annual income tax return shall be filed with the Revenue District Office, Authorized Agent bank, or other proper office which has jurisdiction over the employee's legal residence or principal place of business. It may also be filed with the Revenue District Office or Authorized Agent Bank where the principal office of his/her employer is situated."

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[6] BIR Form No. 1700 for individuals earning purely compensation income and BIR Form No. 1701 for individuals earning both business and compensation income.

Pursuant thereto, petitioners filed, via joint filing, with the BIR Revenue District Office (RDO) No. 41 their annual Income Tax Return[7] (ITR) for taxable year 2013 and paid the total amount of ₱2,121,359.00, broken down in two installments: on March 21, 2014[8], the amount of ₱1,060,680.00 and the remaining amount of ₱1,060,679.00 on July 8, 2014[9].

Thereafter, on March 21, 2016, petitioners filed with the BIR their administrative claim via a Letter Re: Claim for Tax Refund of Erroneously and Illegally Collected Income Tax of Spouses Michael Gavin Richard L. De Los Reyes and Jennifer Chua Co-De Los Reyes for taxable year 2013[10] dated March 17, 2016. Petitioners primarily relied on the case decided by the Regional Trial Court (RTC) Branch 213 of Mandaluyong City entitled, *Erwin Salaveria and Portia Gonzales vs. Commissioner of Internal Revenue, Civil Case No. MC14-8775, September 30, 2014*[11], wherein the RTC declared Section 2 (d)(1) of RMC No. 31-2013 as void for being issued without legal basis, in excess of authority and/or without due process of law. Respondent therein appealed the decision to the Court of Appeals, which was docketed as CA-G.R. CV No. 104374, but was eventually dismissed due to technicality in a Resolution dated July 3, 2015.[12]

On the same day, March 21, 2016, petitioners simultaneously filed with this Court their judicial claim via a Petition for Review[13].

On May 19, 2016, respondent filed his Answer[14] raising the following defenses, viz.:

> "9. She SPECIFICALLY DENIES the material allegations in paragraphs 18, 19, 20, 21, 22 and 23 of the Petition for being false. The truth of the matter is that being Filipino citizens and residents of the Republic of the Philippines, petitioners are subject to income tax;
>
> Sections 23 and 22 (E) of the National Internal Revenue Code of 1997, as amended, specifically states:
>
> '**SEC. 23.** ***General Principles of Income Taxation in the Philippines.*** – Except when otherwise provided in this Code:

[7] Exhibit "4".
[8] Exhibits "P-5", "P-5-a", and "P-5-b".
[9] Exhibits "P-6", "P-6- a", "P-6-b" and "P-7-b".
[10] Exhibits "P-1" and "P-1-a".
[11] Exhibit "P-8".
[12] Exhibit "P-9".
[13] Supra No. 1.
[14] Docket (Vol. I), pp. 148-159.

(A) A citizen of the Philippines residing therein is taxable on all income derived from sources within and without the Philippines; x x x.'

'**SEC. 22. *Definitions.*** – When used in this Title:

x x x

(E) The term '*nonresident citizen*' means;

(1) A citizen of the Philippines who establishes to the satisfaction of the Commissioner the fact of his physical presence abroad with a definite intention to reside therein.

(2) A citizen of the Philippines who leave the Philippines during the taxable year to reside abroad, either as an immigrant or for employment on a permanent basis.

(3) A citizen of the Philippines who works and derives income from abroad and whose employment thereat requires him to be physically present abroad most of the time during the taxable year.

(4) A citizen who has been previously considered as nonresident citizen and who arrives in the Philippines at any time during the taxable year to reside permanently in the Philippines shall likewise be treated as nonresident citizen for the taxable year in which he arrives in the Philippines with respect to his income derived from sources abroad until the date of his arrival in the Philippines.

(5) The taxpayer shall submit proof of the Commissioner to show his intention of leaving the Philippines to reside permanently abroad or to return to and reside in the Philippines as the case may be for purposes of this Section.'

Taxation of income in the Philippines is based on Citizenship, Residency and the Source Principle;

Under the *Citizenship principle*, the basis of the imposition of income tax is the taxpayer's citizenship. All citizens of the Philippines, whether resident or non-resident, are subject to our income tax law. In the case of resident citizens, they are subject to income tax derived from within and without the Philippines, while non-resident citizens are only subject to the income tax on the income derived from within the Philippines;

Under the *Residence principle*, the basis of the imposition of all income tax in this case is the residence of the taxpayer. All income derived by persons residing in the Philippines, whether citizens or aliens, whether domestic corporations or foreign corporations, shall be subject to income tax on the income derived from sources within the Philippines;

Under the *Source Principle*, the basis of the imposition of income tax is the source of the income. All income derived from sources within the Philippines shall be subject to income tax. Thus, even nonresident citizens or aliens and foreign corporations who derive income from within the country are subject to income tax. This also follows the territoriality principle;

Petitioners are Filipino citizens and employees of the Asian Development Bank, with business address at ADB Avenue, Ortigas Center, Mandaluyong City. There is no doubt that Petitioners are liable for income tax on the compensation income they earned on account of such employment;

When the ADB Charter was created in 1965, it was expressly stated in Article 56 on Exemption from Taxation that:

> '*No tax shall be levied on or in respect of salaries and emoluments paid by the Bank to Directors, alternates, officers or employees of the Bank, except where a member deposits with its instruments of ratification or acceptance a declaration that such member retains for itself and its political subdivisions the right to tax salaries and emoluments paid by the Bank to citizens or nationals of such member.*'

In signing the ADB Headquarters Agreement in 1956, the Philippine government accorded tax exemption privileges to the ADB and its staff, but held on to the State's inherent power to tax, and thus made a clear limitation in so far as its right to tax its nationals. Hence, Section 45(b), Article XII of the ADB Headquarters Agreement provides that:

'*Article XII*

PRIVILEGES AND IMMUNITIES OF GOVERNORS AND OTHER REPRESENTATIVES OF MEMBERS,

DIRECTORS, PRESIDENT, VICE-PRESIDENT AND OTHERS

Section 45

Officers and staff of the Bank, including for the purposes of this Article experts and consultants performing missions for the Bank, shall enjoy the following privileges and immunities:

x x x

(b) Exemptions from taxation on or in respect of the salaries and emoluments paid by the Bank subject to the power of the Government to tax its nationals; x x x.'

In the same year, the Philippine Congress issued Resolution No. 06 to the effect that 'the Senate of the Philippines concurs, as it hereby concurs, in the ratification by the President of the Philippines of the aforesaid Agreement Establishing the Asian Development Bank, subject to the ***reservation*** that the Philippines declares that it retains for itself and its political subdivisions the right to tax salaries and emoluments paid by the Bank to its citizens or nationals of the Philippines pursuant to Article 56, paragraph 2, of the Agreement.' (*Underscoring supplied*)

Explicit from the foregoing is that the Philippines, by making a 'reservation', simply intimated *[sic]* that in entering upon an Agreement with ADB the only effect is that the income of ADB is exempt from tax by virtue of the Agreement but not the income derived by the Filipinos from ADB;

Petitioners may claim that the coverage of the Article XII of 'Headquarters Agreement' only concerns the privileges and immunities of the higher officials of the ADB. Such contention is utterly misplaced since the title of the Article itself did not restrict the application of the said Article of ADB's higher officials only, to wit: PRIVILEGES AND IMMUNITIES OF GOVERNOR'S AND OTHER REPRESENTATIVES OF MEMBERS, DIRECTORS, PRESIDENT, VICE-PRESIDENT AND OTHERS;

Moreover, the above-quoted Section 45 of the said Article referred to Officers and Staff of the bank as well;

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BIR ITAD Ruling further states that there is no need for an executing law to implement the 'Reservation' because Philippine tax law already provides that Filipinos are liable for tax from income derived from within and without the Philippines;

The construction of the word 'Reservation' can only be accorded its plain meaning if, before the Philippines entered into the Agreement with ADB, Filipinos earning income from without the Philippines have no obligation to pay taxes in the Philippines. Since 1939, Filipinos earning income derived from outside the Philippines are liable for tax from such income. This is true when one considers Section 37 in relation to Section 45 of the Internal Revenue Code of 1939, Section 21 in relation to Section 27 of the National Internal Revenue Code of 1997, and Section 24 in relation to Section 51 of the National Internal Revenue Code of 1997;

To accord the word 'reservation' with an ordinary meaning will undermine the force of existing tax laws. Thus, a contrary interpretation would mean subverting Philippine sovereignty by virtue of a mere Agreement just for the purpose of exempting some Filipinos from income tax. While international comity is laudable and a Constitutional requirement, the power to tax is an inherent power of the State that cannot be bargained away so easily;

Same BIR ITAD Ruling added that the ADB Charter is not a law, but an agreement among Contracting States. That being the case, it is a derogatory interpretation that exempting from tax includes exemption from tax of Filipino citizens without express mention of Filipino exemption;

Pacta sunt servanda and international comity dictate that the Philippines should honor its international agreements in good faith. The Philippines has arguably complied with these principles of international law by according the proper concessions and tax breaks to ADB activities. This duty ends where the concern is a domestic matter involving the taxability of the income of its citizens. The ADB Charter was never amended by subsequent Philippine tax laws, because Philippine tax laws before and after the creation of ADB imposed taxes on income of Filipinos from within and without the Philippines;

Petitioners may contend that subsequent practice, as regards the ADB charter, is non-taxability of the income of its employees, arguing that ADB employees have never been subjected by the taxing authority ever since the Philippines' ratification of the ADB Charter. They insist that an operative act is required to change the norm followed after the ratification of the ADB Charter;

It is as if Petitioners would like this Honorable Court to treat such subsequent practice into a custom which is recognized source law. It is a standard rule that customs which are contrary to law shall not be countenanced;

In the case of *Malang vs. Moson*, the Supreme Court significantly held that:

> '*The Court is duty-bound to resolve that the instant case applying such laws and rights as are in existence at the time the pertinent civil acts took place, and is unable to supplant governing law with customs, albeit how widely observed.*'

10. She SPECIFICALLY DENIES the material allegations in paragraphs 24, 25, 26 and 27 of the Petition for being false. The truth of the matter is that the Regional Trial Court, Branch 213, Mandaluyong City (RTC Branch 213), has no jurisdiction in taking cognizance of the case filed by the employees of the Asian Development Bank pertaining to the validity of Revenue Memorandum No. 31-2013 (RMC 31-2013);

In the case of *Philippine American Life and General Insurance Company (Philamlife) v. The Secretary of Finance and the Commissioner of Internal Revenue*, the Supreme Court ruled that:

> 'Evidently, *City of Manila* can be considered as a departure from *Ursal* in that in spite of there being no express grant in law, the CTA is deemed granted with powers of certiorari by implication. Moreover, *City of Manila* diametrically opposes *British American Tobacco* to the effect that it is now within the power of the CTA, through its power of certiorari, to rule on the validity of a particular administrative rule or regulation so long as it is within its appellate jurisdiction. **Hence, it can now rule not only on the propriety of an assessment or tax treatment of a certain transaction, but also on the validity of the revenue regulation or revenue memorandum circular on which the said assessment is based.**'

RMC 31-2013 is only a clarification of existing policies already in the law. Thus, this alleged subsequent practice, which is contrary to existing law, cannot in any way displace what the law had provided from the start;

RMC 13-2013 is valid because it is only a mere clarification of existing policies embodied in the law;

As stated in BIR ITAD Ruling No. 018-14, the 'Reservation' made by the Philippines regarding its right to tax its citizen who earn income as employees of ADB is not a mere reservation but an affirmation of the inherent power of the State to tax its own citizens;

Petitioners anchor their claim that they are exempted from income tax on the provisions of Revenue Memorandum Order No. 31-2013 which provides:

x x x

(d) Those Employed by Organizations Covered by Separate International Agreements or Specific Provisions of Law –

1. Asian Development Bank (ADB)

Section 45(b), Article XII of the Agreement between the Asian Development Bank and the Government of the Republic of the Philippines regarding the Headquarters of the Asian Development Bank provides:

'ARTICLE XII

x x x

Section 45

<u>Officers and staff of the Bank, including for the purposes of this Article experts and consultants performing missions for the Bank</u>, shall enjoy the following privileges and immunities:

x x x

(b) Exemption from taxation on or in respect of the salaries and emoluments paid by the Bank <u>subject to the power of the Government to tax its nationals</u>;'

From the above, only officers and staff of the ADB who are not Philippine nationals shall be exempt from Philippine income tax.

Petitioners claim that they are exempt from the payment of income tax has no legal basis. Under the above-cited revenue issuance, it is clear that the exemption is still subject to the power of the Government to tax its nationals, including herein Petitioners. Thus, reverting to the earlier discussion, Section 23, in relation to Section 24 of the National Internal Revenue Code of 1997, as amended, are the laws on the matter. As previously submitted, Petitioners, being Filipino citizens and nationals are taxable from their income within and outside the Philippines;

11. Petitioners must prove that they were able to comply with the following documentary and legal requirements as provided under Section 229 of the National Internal Revenue Code, as amended, to wit:

> a) That the taxpayer should file a written claim for refund or tax credit with the BIR Commissioner within two (2) years from the date of payment of the tax or penalty, non-compliance with which the latter is precluded from exercising his authority thereon;
>
> b) That, if denied or not acted upon within said period, the petition for refund be filed with the CTA within 30 days from receipt of the denial AND within said two (2) year period from the date of payment of the tax or penalty regardless of any supervening cause, otherwise, the claim for refund shall have prescribed;
>
> (c) The claim for refund must be a categorical demand for reimbursement;
>
> (d) There must be a proof or payment of the erroneously or illegally collected taxes; and
>
> (e) No refund shall be given resulting from availment of incentives granted pursuant to special laws for which no actual payment was made.

Petitioners must prove that their income is not taxable or exempt from income tax;

Petitioners must provide the basis for the alleged tax exemptions;

Tax exemptions are never presumed and are strictly construed against the taxpayer and liberally in favor of the taxing authority. They can only be given force when the grant is clear and categorical. The surrender of the power to tax, when claimed must be clearly shown by a language that will admit of no reasonable construction consistent with the reservation of the power. If the intention of the legislature is open to doubt, then the intention of the legislature must be resolved in favor of the State. *(Smart Communications, Inc. vs. The City of Davao, et al G.R. No. 155491)*

A tax refund is in the nature of a tax exemption which must be construed *strictissimi juris* against the taxpayer. The taxpayer must present convincing evidence to substantiate a claim for refund. (*FEBTC vs. CIR, G.R. No. 149589, September 16, 2006*)

In the case of *CIR vs. Rosemarie Acosta, G.R. 154068 dated August 3, 2007*, the Honorable Supreme Court ruled, to wit:

'As tax refunds involve a return of revenue from the government, the claimant must show indubitably the specific provision of law from which her right arises, it cannot be allowed to exist upon a mere vague implication or inference nor can it be extended beyond the ordinary and reasonable intendment of the language actually used by the legislature in granting the refund. To repeat, strict compliance with the conditions imposed for the return of revenue collected is a doctrine consistently applied in this jurisdiction.'"

Thereafter, on May 20, 2016, a Notice of Pre-Trial Conference[15] was issued by this Court, setting the case for pre-trial conference on September 20, 2016 at 9:00 a.m. The parties were ordered, among others, to be present and file their respective Pre-Trial Briefs at least three (3) days before the date of pre-trial.

In compliance, Respondent's Pre-Trial Brief[16] was filed on September 15, 2016, while petitioners submitted their Pre-Trial Brief[17] on September 16, 2016.

On September 30, 2016, the parties filed their Joint Stipulation of Facts and Issues[18] (JSFI). As such, on November 8, 2016, this Court issued a Pre-Trial Order[19], adopting the parties' JSFI and thereafter deemed pre-trial terminated.

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[15] *Ibid*, pp. 160-161.
[16] *Id.*, pp. 167-169.
[17] *Id.*, pp. 299-310.
[18] *Id.*, pp. 319-327.
[19] *Id.*, pp. 337-342.

The initial presentation of evidence for the petitioners was then set on November 21, 2016 at 1:30 p.m.

After which, trial ensued.

For its witnesses, counsel for petitioners submitted on September 16, 2016, the testimony of Michael Gavin Richard L. De Los Reyes by way of Judicial Affidavit[20]. While, Jennifer C. Co-De Los Reyes' Judicial Affidavit[21] was submitted on January 11, 2017.

There being no more witness, petitioners filed their Formal Offer of Documentary Evidence[22] on January 27, 2017, offering Exhibits "P-1" to "P-13-a" as their documentary evidence. Consequently, in the Resolution[23] dated September 4, 2017, this Court admitted petitioners' exhibits except for Exhibits "P-2", "P-3" and "P-8" for petitioners' failure to present the original documents for comparison.

On September 26, 2017, petitioners filed, through registered mail, a Motion for Partial Reconsideration (Of the Resolution dated 4 September 2017)[24]. Petitioners claim that Exhibits "P-2" and "P-3" are original computer print-outs which is considered originals pursuant to Administrative Matter No. 01-7-01-SC on the Rules on Electronic Evidence, while Exhibit "P-8" is the Decision rendered by the RTC Branch 213 of Mandaluyong City entitled, *Erwin Salaveria and Portia Gonzales vs. Commissioner of Internal Revenue, Civil Case No. MC14-8775, September 30, 2014*. Petitioners explain that Exhibit "P-8" was actually secured from the Court of Appeals' Archives Section. Thus, petitioners pray that the said exhibits be reconsidered and admitted by this Court.

In the Resolution[25] dated January 8, 2018, this Court found merit in petitioners' Motion thereby admitting Exhibits "P-2", "P-3" and "P-8". Moreover, the initial presentation of evidence for the respondent was set on January 15, 2018 at 1:30 p.m.

During his initial presentation of evidence, counsel for respondent manifested that he has no evidence to present.[26] Thus, the parties were given period of thirty (30) days or until February 14, 2018 within which to submit their respective memoranda.

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[20] *Id.*, pp. 173-182.
[21] *Id.*, pp. 349-358.
[22] *Id.*, pp. 480-487.
[23] Docket (Vol. II), pp. 877-878.
[24] *Ibid*, pp. 882-887.
[25] *Id.*, pp. 895-896.
[26] Minutes of the Hearing dated January 15, 2018, *id.*, p. 897.

On February 12, 2018, respondent filed a Manifestation[27] stating that he is adopting the arguments in his Answer as his Memorandum, while petitioners filed, on the other hand, their Memorandum[28] on February 14, 2018.

Accordingly, in the Resolution[29] dated February 22, 2018, the instant case was deemed submitted for decision.

THE ISSUES

The sole issue[30] to be resolved by this Court is whether or not petitioners are entitled to a refund of the income tax on compensation they received from the ADB for the taxable year 2013.

THE RULING OF THE COURT

This Court shall first determine petitioners' compliance with the procedures governing the filing of claims for refund under Sections 204 (C) and 229 of the National Internal Revenue Code (NIRC) of 1997, as amended, in relation to Section 3(a)(2) of the Revised Rules of the Court of Tax Appeals (RRCTA), which respectively reads as follows:

> "**SECTION 204.** *Authority of the Commissioner to Compromise, Abate and Refund or Credit Taxes.* – The Commissioner may –
>
> x x x
>
> (C) Credit or refund taxes erroneously or illegally received or penalties imposed without authority, refund the value of internal revenue stamps when they are returned in good condition by the purchaser, and, in his discretion, redeem or change unused stamps that have been rendered unfit for use and refund their value upon proof of destruction. No credit or refund of taxes or penalties shall be allowed unless the taxpayer files in writing with the Commissioner a claim for credit or refund within two (2) years after the payment of the tax or penalty: *Provided, however,* That a return filed showing an overpayment shall be considered as a written claim for credit or refund."
>
> "**SEC. 229.** *Recovery of Tax Erroneously or Illegally Collected.* – No suit or proceeding shall be maintained in any court for the recovery of any national internal revenue tax hereafter alleged to have been

[27] *Id.*, pp. 899-901.
[28] *Id.*, pp. 902-918.
[29] *Id.*, p. 921.
[30] Statement of Issues, JSFI, Docket (Vol. I), p. 320.

erroneously or illegally assessed or collected, or of any penalty claimed to have been collected without authority, or of any sum alleged to have been excessively or in any manner wrongfully collected, until a claim for refund or credit has been duly filed with the Commissioner; but such suit or proceeding may be maintained, whether or not such tax, penalty, or sum has been paid under protest or duress.

In any case, no such suit or proceeding shall be filed after the expiration of two (2) years from the date of payment of the tax or penalty regardless of any supervening case that may arise after payment: *Provided, however,* That the Commissioner may, even without a written claim therefor, refund or credit any tax, where on the face of the return upon which payment was made, such payment appears clearly to have been erroneously paid." *(Emphasis Supplied)*

"**SEC. 3.** *Cases within the jurisdiction of the Court in Division.* – The Court in Division shall exercise:

(a) **Exclusive original over or appellate jurisdiction to review by appeal** the following:

x x x

> (2) **Inaction by the Commissioner of Internal Revenue in cases involving** disputed assessments, **refunds of internal revenue taxes fees or other charges**, penalties in relation thereto, or other matters arising under the National Internal Revenue Code or other laws administered by the Bureau of Internal Revenue, where the National Internal Revenue Code or other applicable law provides a specific period for action: *Provided*, that in case of disputed assessments, the inaction of the Commissioner of Internal Revenue within the one hundred eighty day-period under Section 228 of the National Internal Revenue Code shall be deemed a denial for purposes of allowing the taxpayer to appeal his case to the court and does not necessarily constitute a formal decision of the Commissioner of Internal Revenue on the tax case; *Provided further*, that should the taxpayer opt to await the final decision of the Commissioner of Internal Revenue on the disputed assessments beyond the one hundred eighty day-period above-mentioned, the taxpayer may appeal such final decision to the Court under Section 3(a), Rule 8 of these Rules; and *Provided, still further*, **that in the case of claims for refund of taxes erroneously or illegally collected, the taxpayer must file a petition for review with the Court prior to the expiration of the two-year period under Section 229 of the National Internal Revenue Code**;" *(Emphases Supplied)*

Based on the above-quoted provisions, both administrative and judicial claims must be filed within two (2) years from the date of payment of the tax. Section 204 (C) of the NIRC of 1997, as amended, applies to administrative claims filed with the BIR, while Section 229 of the NIRC of 1997, as amended, in relation to Section 3(a)(2) of the RRCTA both refers to judicial actions for the recovery of taxes erroneously or illegally collected and filed with the court.

In the instant case, records show that petitioners paid their income taxes for 2013 on installment on March 21, 2014[31] and July 8, 2014[32]. Plethora of jurisprudence[33] dictates that when a tax is paid on an installment basis, the computation of the two-year prescriptive period should be from the date of the last installment or final payment.

Applying the foregoing, since both administrative and judicial claims for refund were filed on March 21, 2016, this Court deemed the claims to have been seasonably filed within the two-year period provided by the above-mentioned provisions.

That having been settled, this Court shall now proceed to review the applicable treaty and legislative provisions addressing the tax treatment of income of petitioners as employees of the ADB.

Since the onset, petitioners aver that under the agreement establishing the ADB Charter, ADB employees are exempt from income tax. As such, petitioners argue that RMC No. 31-2013, which explicitly states that only ADB employees who are not Philippine nationals are exempt from income tax, is null and void for being issued without factual and legal basis and in violation of due process of law.

The Court remains unconvinced.

Verily, Article 56 of the ADB Charter[34] provides tax exemption privileges to certain members of the ADB, the relevant provision is quoted hereafter as follows, viz.:

"Article 56

EXEMPTION FROM TAXATION

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[31] Supra No. 8.

[32] Supra No. 9.

[33] *Atlas Consolidated Mining and Development Corporation vs. Commissioner of Internal Revenue*, G.R. Nos. 141104 and 148763, June 8, 2007; *Collector of Internal Revenue vs. Prieto*, et al., G.R. No. L-11976, August 29, 1961; *Commissioner of Internal Revenue vs. Palanca, Jr.*, G.R. No. L-16626, October 29, 1966.

[34] "THE AGREEMENT ESTABLISHING THE ASIAN DEVELOPMENT BANK", December 4, 1965.

> 1. The Bank, its assets, property, income and its operations and transactions, shall be exempt from all taxation and from all customs duties. The Bank shall also be exempt from any obligation for the payment, withholding or collection of any tax or duty.
>
> 2. **No tax shall be levied on or in respect of salaries and emoluments paid by the Bank to Directors, alternates, officers or employees of the Bank**, including experts performing missions for the Bank, **except where a member deposits with its instrument of ratification or acceptance a declaration that such member retains for itself and its political subdivisions the right to tax salaries and emoluments paid by the Bank to citizens or nationals of such member**." (*Emphases Supplied*)

Thereafter, in Senate Resolution No. 6 dated March 16, 1966, the ADB Charter was ratified and confirmed by the Philippine Government with a reservation of its right to tax the Filipino employees of the ADB, to wit:

> "NOW THEREFORE, be it known that I, FERDINAND E. MARCOS, President of the Republic of the Philippines, having seen and considered the Agreement Establishing the Asian Development Bank done on December 4, 1965 at Manila, Philippines, do hereby in pursuance of the aforesaid concurrent of the Senate of the Philippines, ratify and confirm the said Agreement and every article and clause thereof, **subject to the reservation that the Philippines declares that it retains for itself and its political subdivision the right to tax salaries and emoluments paid by the Bank to citizens or nationals of the Philippines**." (*Emphasis Supplied*)

On December 22, 1966, the *"Agreement Between the Asian Development Bank and the Government of the Republic of the Philippines Regarding the Headquarters of the Asian Development Bank"* ("ADB Headquarters Agreement" for brevity) was signed, and included a similar provision recognizing the right of the Philippine Government to tax Filipino ADB employees, in this wise:

> "ARTICLE XII
> Privileges and Immunities of Governors and Other Representatives of Members, Directors, President, Vice-President and Others
>
> x x x
>
> Section 45.

Officers and staff of the Bank, including for the purposes of this Article experts and consultants performing missions for the Bank, **shall enjoy the following privileges and immunities**:

(a) Immunity from legal process with respect to acts performed by them in their official capacity except when the Bank waives the immunity;

(b) **Exemption from taxation** on or in respect of the salaries and emoluments paid by the Bank **subject to the power of the Government to tax its nationals** xxx." (*Emphases Supplied*)

From the foregoing, while it is true that the ADB Charter provides a tax exemption provision with respect to the salaries and emoluments paid by the ADB to its officers and employees, the same, however, also contains a proviso wherein a member-country, like the Philippines, may opt to retain its right to tax the salaries and emoluments paid by the ADB to its citizens or nationals. Stated differently, if the Philippine Government really intended to exempt from income taxation the salaries or emoluments that its citizens or nationals would receive from the ADB, a full ratification of the ADB Charter should have been made, without retaining its right to tax its citizens or nationals, or any reservation whatsoever to that effect.

Basic is the rule in statutory construction that every part of the statute must be interpreted with reference to the context, *i.e.*, that every part of the statute considered together with the other parts, and kept subservient to the general intent of the whole enactment. Because the law must not be read in truncated parts, its provisions must be read in relation to the whole law. The statute's clauses and phrases must not, consequently, be taken as detached and isolated expressions, but the whole and every part thereof must be considered in fixing the meaning of any of its parts in order to produce a harmonious whole.[35]

Accordingly, the exemption granted to officers and employees of the ADB pursuant to the ADB Charter and the ADB Headquarters Agreement must not be read in isolation as there is a *proviso* subjecting Philippine nationals to tax imposed by the Philippine Government on income received from the bank.

More so, the current tax code – the NIRC of 1997, as amended, a subsequent legislation which took effect on January 1, 1998, is the law that enables the enforcement of the reservation clauses found in Senate Resolution No. 6 and Section 45(b) of the ADB Headquarters Agreement. As a matter of fact, Sections 23(A) and 24(A)(1)(a) of the NIRC of 1997, as amended, left no

[35] *Commissioner of Internal Revenue vs. Pilipinas Shell Petroleum Corporation*, G.R. No. 192398, September 29, 2014.

room for doubt that resident citizens are subject to tax on income derived from all sources within and without the Philippines, to wit:

> "**SEC. 23.** *General Principles of Income Taxation in the Philippines.* – Except when otherwise provided in this Code:
>
> (A) **A Citizen of the Philippines residing therein is taxable on all income derived from sources within and without the Philippines**;
>
> x x x." *(Emphasis Supplied)*
>
> "**SEC. 24.** *Income Tax Rates.* –
>
> (A) *Rates of Income Tax on Individual Citizen and Individual Resident Alien of the Philippines.* –
>
> (1) An income tax is hereby imposed:
>
> (a) On the taxable income defined in Section 31 of this Code, other than income subject to tax under Subsections (B), (C) and (D) of this Section, derived for each taxable year **from all sources within and without the Philippines by every individual citizen of the Philippines residing therein**;" *(Emphasis Supplied)*

Evidently, the above-quoted provisions impose tax on the income of resident individual citizens from all sources **within and without** the Philippines. Henceforth, in the absence of a specific grant of tax exemption, the salaries and emoluments received by Filipino employees of the ADB are subject to income tax.

Furthermore, in the case entitled *Spouses Michael Gavin Richard L. de los Reyes and Jennifer C. Co-de los Reyes vs. Commissioner of Internal Revenue*[36], where petitioners in the present case are the same parties therein, this Court ordered the refund of the income tax paid by petitioners for calendar year 2012. This Court held that it would be in keeping with justice and equity for the implementation of RMC No. 31-2013 to begin prospectively and to apply to compensation income earned by petitioners beginning CY 2013, thus:

[36] CTA Case No. 9088, October 19, 2017.

"While it can be argued that RMC No. 31-13 is a mere interpretation of existing law and should thus be applied even to the compensation income of petitioners for CY 2012, the Court holds that it should be applied prospectively in the interest of justice and equity. Consequently, the income of resident citizens employed by foreign governments and/or international organizations should only be subjected to income tax beginning CY 2013, the year RMC No. 31-13 took effect.

In the present case, petitioners received the compensation income being subject to income tax in CY 2012. During this period, petitioners were of the honest belief — and neither did respondent enforce rules to the contrary — that their compensation income was exempt from tax. When respondent issued RMC No. 31-13 and sought to enforce its provisions subjecting compensation income of resident citizens employed by ADB to the graduated income tax rates immediately, petitioners were constrained to file their Joint ITR for CY 2012 and pay the aggregate amount of Php1,948,832.34 in one payment. Whereas previously, petitioners' incomes were not subjected to tax, they now had to come up with approximately Php2,000,000.00 — a substantial amount — to settle their income tax liabilities. Hence, it would be in keeping with justice and equity for the implementation of RMC No. 31-13 to begin prospectively and to apply to compensation income earned by petitioners beginning CY 2013.

In sum, compensation income of resident citizens is subject to the graduated income tax rates unless expressly exempted under treaty. With the Philippines' reservation in the ADB Charter to the effect that it maintains the right to subject to income tax the compensation of resident citizens employed by the ADB, the rule then is that resident citizens employed by foreign governments and/or international organizations, such as ADB, are subject to the graduated income tax rates under Section 24 (A) of the 1997 NIRC. However, considering RMC No. 31-13 was issued in CY 2013, the same should be made to apply prospectively in the interest of justice and equity. Hence, compensation income of resident citizens employed by foreign governments and/or international organizations shall only be subject to income tax beginning CY 2013."

Also, in the similar cases of *Leah Empesando, et al. vs. Commissioner of Internal Revenue*[37] and *Erwin Casaclang vs. Commissioner of Internal Revenue (RDO 041 Mandaluyong City)*[38], this Court likewise held that the income of resident citizens employed by foreign governments and/or international organizations should

[37] CTA Case No. 9093, September 17, 2013.

[38] CTA Case No. 9091, August 6, 2018.

only be subjected to income tax beginning calendar year 2013, the year RMC No. 31-2013 took effect.

In view of the foregoing, considering that the instant case pertains to compensation income earned by petitioners in the calendar year 2013 – the year that RMC No. 31-2013 has already taken effect, this Court finds that there is no erroneous payment of taxes made in the instant case.

WHEREFORE, premises considered, the instant Petition for Review is **DENIED** for lack of merit.

SO ORDERED.

MA. BELEN M. RINGPIS-LIBAN
Associate Justice

I CONCUR:

ESPERANZA R. FABON-VICTORINO
Associate Justice

ATTESTATION

I attest that the conclusions in the above decision were reached in consultation before the case was assigned to the writer of the opinion of the Court's Division.

ESPERANZA R. FABON-VICTORINO
Associate Justice
Acting Chairperson

CERTIFICATION

Pursuant to Section 13 of Article VIII of the Constitution, and the Acting Division Chairperson's Attestation, it is hereby certified that the conclusions in the above Decision were reached in consultation before the case was assigned to the writer of the opinion of the Court's Division.

ROMAN G. DEL ROSARIO
Presiding Justice