REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

THIRD DIVISION

AUSTRALIA AND NEW ZEALAND BANKING GROUP LIMITED, PHILIPPINES BRANCH, BDO UNIBANK, INC., CHINA BANKING CORPORATION, CITIBANK, N.A., PHILIPPINE BRANCH, CTBC BANK (PHILIPPINES) CORP., DEUTSCHE BANK AG MANILA BRANCH, DEUTSCHE KNOWLEDGE SERVICES PTE. LTD., HONGKONG AND SHANGHAI BANKING CORPORATION LIMITED - PHILIPPINE BRANCH, ING BANK N.V., MANILA BRANCH, JPMORGAN CHASE BANK, N.A. – MANILA BRANCH, MAYBANK PHILIPPINES, INC., RIZAL COMMERCIAL BANKING CORPORATION, SECURITY BANK CORPORATION, SUMITOMO MITSUI BANKING CORPORATION – MANILA BRANCH, STANDARD CHARTERED BANK, AND UNION BANK OF THE PHILIPPINES,
Petitioners,

CTA Case No. SCA-0018

-versus-

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

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BANCNET INCORPORATED, *Petitioner,*	**CTA Case No. SCA-0020** Members:
-versus-	**MANAHAN**, *Chairperson,* **REYES-FAJARDO,** *and* **ANGELES,** *JJ.*
COMMISSIONER OF INTERNAL REVENUE, *Respondent.*	Promulgated: NOV 11 2024 3:24 p.m.

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R E S O L U T I O N

For resolution of the Court are the following:

(1) Petitioners' **Petition for Certiorari and/or Prohibition with Application for a Temporary Restraining Order and/or Writ of Preliminary Injunction and Issuance of Confidentiality Order** in CTA Case No. SCA-0018, filed on March 8, 2024, with respondent's **Comment/Opposition Re: Petitioners' Petition for Certiorari and/or Prohibition with Application for a Temporary Restraining Order and/or Writ of Preliminary Injunction and Issuance of Confidentiality Order** filed on July 5, 2024; and

(2) Petitioner's **Petition for Certiorari and/or Prohibition With [a] Application for a Temporary Restraining Order and/or Writ of Preliminary Injunction; [b] Issuance of Confidentiality Order; and [c] Consolidation** in CTA Case No. SCA-0020, filed on May 8, 2024, with respondent's **Comment with Manifestation [Re: (a) Petitioner's Application for a Temporary Restraining Order and/or Writ of Preliminary Injunction; (b) Application for Confidentiality Order; and (c) Application for Consolidation]**, filed on July 2, 2024.

In CTA SCA No. 0018, petitioners argue that:

A. Respondent violated the constitution by usurping on legislative functions and amending the Tax Code and disregarding tax treaties without authority of law:

A.1 Respondent introduced the "Benefits-Received Principle" in disregard of the "Place of Performance Rule", which is currently found in Section 42 of the Tax Code and has been the rule since 1939;

A.2 Respondent expanded the enumerated services of non-residents subject to Withholding Value-Added Tax (WVAT), contrary to the plain reading of Section 114(C) and Section 105 of the Tax Code;

A.3 Respondent disregarded the Philippines' existing tax treaty obligation to exempt from tax business profits of foreign persons with no permanent establishment in the Philippines;

B. Respondent violated the Constitution by usurping the President's authority in the conduct of foreign relations by his immediate implementation of Pillar I Commitments without the benefit of the thresholds and in the absence of implementing legislation;

C. Respondent violated the Constitution by unduly expanding the interpretation of the *Aces* case and in so doing, usurped judicial functions;

D. Respondent violates the constitutional right to presumption of innocence by creating a presumption of tax evasion in a manner inconsistent with Sections 50, 254, and 255 of the Tax Code; and

E. Revenue Memorandum Circular (RMC) No. 5-2024 is vague, overboard, oppressive, confiscatory, and respondent's selective implementation leads to equal protection of law violation.

Meanwhile, petitioner in CTA Case No. SCA-0020 argues that:

A. RMC No. 38-2004 is vague, overboard, oppressive, confiscatory, and respondent's selective implementation leads to equal protection of law violation.

B. The respondent violated the Constitution by usurping on legislative functions and amending the Tax Code and disregarding tax treaties without authority of law.

B.1 Respondent introduced the "benefits-received principle" in disregard of the "place of performance rule", which is currently found in Section 42 of the Tax Code and has been the rule since 1939.

B.2 Respondent expanded the enumerated services of non-residents subject to withholding VAT, contrary to the plain reading of Section 114(C) and Section 105 of the Tax Code.

B.3 Respondent disregarded the Philippines' existing tax treaty obligation to exempt from tax business profits of foreign persons with no permanent establishment in the Philippines.

B.4 Respondent improperly used parts of Article 1233 of the Civil Code to justify the use of the "benefits received principle" test.

C. The respondent violated the Constitution by usurping the President's authority in the conduct of foreign relations by his immediate implementation of Pillar I Commitments without the benefit of the thresholds and in the absence of implementing legislation.

D. The respondent violated the Constitution by unduly expanding the interpretation of the *Aces* case and in so doing, usurped judicial functions.

On the other hand, respondent in CTA Case No. SCA-0018 counters that: (1) The Court of Tax Appeals (CTA) has no jurisdiction over the instant case; (2) In the alternative that the CTA will acquire jurisdiction, petitioner failed to exhaust administrative remedies before elevating the case to the CTA; (3) In the alternative that the CTA will acquire jurisdiction, petitioner failed to comply with the requisites under Rule 65 of the Rules of Court (ROC) that there is no appeal, or any plain, speedy, and adequate remedy available in the course of law; (4) In the alternative that the CTA has jurisdiction, petitioner failed to comply with Section 3, Rule 46 in relation to Rule 65 of the ROC; and (5) Assuming that the CTA has jurisdiction over the instant case, petitioner has no legal right to be protected.

After careful evaluation of the arguments of both parties, the Court partially agrees with respondent.

The CTA may take cognizance of cases directly challenging the constitutionality or validity of a tax law or

regulation or administrative issuance, *i.e.*, RMC

Respondent argues that the power to determine the validity of an administrative issuance lies within the courts of general jurisdiction. Moreover, since the subject RMC was issued by respondent in the exercise of his quasi-legislative power and not of his quasi-judicial power, the CTA has no jurisdiction to determine the validity of the same.

The Court disagrees with respondent.

Section 7 of Republic Act (RA) No. 1125, as amended, provides for the "other matters" jurisdiction of the CTA. Thus:

> Section 7. Jurisdiction - The CTA shall exercise:
>
> (a) Exclusive appellate jurisdiction to review by appeal, as herein provided:
>
> 1) Decisions of 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**;
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> 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 provides a specific period of action, in which case the inaction shall be deemed a denial;
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> 3) Decisions, orders or resolutions of the Regional Trial Courts in local tax cases originally decided or resolved by them in the exercise of their original or appellate jurisdiction;
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> 4) Decisions of the Commissioner of Customs in cases involving liability for customs duties, fees or other money charges, seizure, detention or release of property affected, fines, forfeitures or other penalties in relation thereto, or other matters arising under the Customs Law or other laws administered by the Bureau of Customs;

5) Decisions of the Central Board of Assessment Appeals in the exercise of its appellate jurisdiction over cases involving the assessment and taxation of real property originally decided by the provincial or city board of assessment appeals;

6) Decisions of the Secretary of Finance on customs cases elevated to him automatically for review from decisions of the Commissioner of Customs which are adverse to the Government under Section 2315 of the Tariff and Customs Code;

7) Decisions of the Secretary of Trade and Industry, in the case of nonagricultural product, commodity or article, and the Secretary of Agriculture in the case of agricultural product, commodity or article, involving dumping and countervailing duties under Sections 301 and 302, respectively, of the Tariff and Customs Code, and safeguard measures under Republic Act No. 8800, where either party may appeal the decision to impose or not to impose said duties." *(Emphasis supplied)*

In relation to the above-quoted provision, the Supreme Court categorically stated in *Banco de Oro, et al. v. Republic of the Philippines, et al.*,[1] that the CTA may take cognizance of cases directly challenging the constitutionality or validity of a tax law or regulation or administrative issuance. Thus:

> "The Court of Tax Appeals has undoubted jurisdiction to pass upon the constitutionality or validity of a tax law or regulation when raised by the taxpayer as a defense in disputing or contesting an assessment or claiming a refund. It is only in the lawful exercise of its power to pass upon all matters brought before it, as sanctioned by Section 7 of Republic Act No. 1125, as amended.
>
> This Court, however, declares that **the Court of Tax Appeals may likewise take cognizance of cases directly challenging the constitutionality or validity of a tax law or regulation or administrative issuance** (revenue orders, revenue memorandum circulars, rulings).
>
> Section 7 of Republic Act No. 1125, as amended, is explicit that, except for local taxes, appeals from the decisions of quasi-judicial agencies (Commissioner of Internal Revenue, Commissioner of Customs, Secretary of Finance, Central Board of Assessment Appeals, Secretary of Trade and Industry) on tax-related problems must be brought *exclusively* to the Court of Tax Appeals.

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[1] G.R. No. 198756, August 16, 2016.

> In other words, within the judicial system, the law intends the Court of Tax Appeals to have exclusive jurisdiction to resolve all tax problems. Petitions for writs of *certiorari* against the acts and omissions of the said quasi-judicial agencies should, thus, be filed before the Court of Tax Appeals.
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> Republic Act No. 9282, a special and later law than Batas Pambansa Blg. 129 provides an exception to the original jurisdiction of the Regional Trial Courts over actions questioning the constitutionality or validity of tax laws or regulations. Except for local tax cases, actions directly challenging the constitutionality or validity of a tax law or regulation or administrative issuance may be filed directly before the Court of Tax Appeals.
>
> Furthermore, **with respect to administrative issuances** (revenue orders, **revenue memorandum circulars**, or rulings), these are issued by the Commissioner under its power to make rulings or opinions in connection with the implementation of the provisions of internal revenue laws. Tax rulings, on the other hand, are official positions of the Bureau on inquiries of taxpayers who request clarification on certain provisions of the National Internal Revenue Code, other tax laws, or their implementing regulations. Hence, **the determination of the validity of these issuances clearly falls within the exclusive appellate jurisdiction of the Court of Tax Appeals under Section 7(1) of Republic Act No. 1125, as amended, subject to prior review by the Secretary of Finance, as required under Republic Act No. 8424**." *(Emphasis supplied)*

Applying the *Banco de Oro* case, in relation to Section 7 of RA No. 1125, as amended, the CTA has exclusive appellate jurisdiction to determine the validity of an RMC. Hence, the Court finds respondent's argument untenable.

While the CTA has jurisdiction to determine the validity of an RMC, the Court cannot exercise the same for failure of petitioners to exhaust administrative remedies

On this score, Section 4 of the 1997 National Internal Revenue Code (NIRC), as amended, pertinently provides:

> "**Section 4**. *Power of the Commissioner to Interpret Tax Laws and to Decide Tax Cases.* - The power to interpret the

> provisions of this Code and other tax laws shall be under the exclusive and original jurisdiction of the Commissioner, **subject to review by the Secretary of Finance**."

Relatively, Sections 2 and 3 of Department of Finance (DOF) Department Order No. 007-02 pertinently provide:

> "SECTION 2. *Validity of Rulings.* — A ruling by the Commissioner of Internal Revenue shall be presumed valid until overturned or modified by the Secretary of Finance."
>
> "SECTION 3. *Rulings Adverse to the Taxpayer.* — A taxpayer who receives an adverse ruling from the Commissioner of Internal Revenue may, within thirty (30) days from the date of receipt of such ruling, seek its review by the Secretary of Finance. Xxx"

Section 4 of the 1997 NIRC provides that the interpretation of tax laws is under the exclusive and original jurisdiction of respondent, *subject to review by the Secretary of Finance.* On the other hand, Sections 2 and 3 of DOF Department Order No. 007-02 provides the procedure for the review by the Secretary of Finance.

The importance of exhaustion of administrative remedies, *i.e.*, review by the Secretary of Finance, has been emphasized by the Supreme Court in various cases. Thus:

> In *Asia International Auctioneers, Inc. and Subic Bay Motors Corporation v. Hon. Guillermo L. Parayno, et al.*,[2] the Supreme Court held that "[I]t is settled that the premature invocation of the court's intervention is fatal to one's cause of action. If a remedy within the administrative machinery can still be resorted to by giving the administrative officer every opportunity to decide on a matter that comes within his jurisdiction, then such remedy must first be exhausted before the court's power of judicial review can be sought. The party with an administrative remedy must not only initiate the prescribed administrative procedure to obtain relief but also pursue it to its appropriate conclusion before seeking judicial intervention in order to give the administrative agency an opportunity to decide

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[2] G.R. No. 163445, December 18, 2007.

the matter itself correctly and prevent unnecessary and premature resort to the court."[3]

In the case of *The Philippine American Life and General Insurance Company v. The Secretary of Finance and the Commissioner of Internal Revenue (Philam)*,[4] the Supreme Court explained the taxpayer's remedy adversely affected by respondent's power to interpret under Section 4 of the 1997 NIRC, as amended, as follows:

> "Preliminarily, it bears stressing that there is no dispute that what is involved herein is the respondent Commissioner's exercise of power under the first paragraph of Sec. 4 of the NIRC—the power to interpret tax laws. This, in fact, was recognized by the appellate court itself, but **erroneously held that her action in the exercise of such power is appealable directly to the CTA. As correctly pointed out by petitioner, Sec. 4 of the NIRC readily provides that the Commissioner's power to interpret the provisions of this Code and other tax laws is subject to review by the Secretary of Finance**. The issue that now arises is this—where does one seek immediate recourse from the adverse ruling of the Secretary of Finance in its exercise of its power of review under Sec. 4?
>
> Admittedly, there is no provision in law that expressly provides where exactly the ruling of the Secretary of Finance under the adverted NIRC provision is appealable to. However, We find that Sec. 7(a)(1) of RA 1125, as amended, addresses the seeming gap in the law as it vests the CTA, albeit impliedly, with jurisdiction over the CA petition as 'other matters' arising under the NIRC or other laws administered by the BIR. As stated:
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> Sec. 7. Jurisdiction.- The CTA shall exercise:
>
> a. Exclusive appellate jurisdiction to review by appeal, as herein provided:
>
> 1. Decisions of the Commissioner of Internal Revenue in cases involving disputed assessments, refunds of internal revenue

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[3] *Id.*, citing *National Irrigation Administration v. Enciso*, G.R. No. 142571, May 5, 2006, 489 SCRA 570, 576; *Metro Drug Distribution, Inc. v. Metro Drug Corporation Employees Association-Federation of Free Workers*, G.R. No. 142666, September 26, 2005, 471 SCRA 45, 58 citing *Ambil, Jr. v. Commission on Elections*, G.R. No. 143398, 25 October 2000, 344 SCRA 372; *Zabat v. CA*, G.R. No. 122089, August 23, 2000, 338 SCRA 551, 560 citing *Jariol v. Commission on Elections*, G.R. No. 127456, March 20, 1997, 270 SCRA 255, 262.

[4] G.R. No. 210987, November 24, 2014.

> taxes, fees or other charges, penalties in relation thereto, or other matters arising under the National Internal Revenue or other laws administered by the Bureau of Internal Revenue.
>
> Even though the provision suggests that it only covers rulings of the Commissioner, *We* hold that it is, nonetheless, sufficient enough to include appeals from the Secretary's review under Sec. 4 of the NIRC.
>
> It is axiomatic that laws should be given a reasonable interpretation which does not defeat the very purpose for which they were passed. Courts should not follow the letter of a statute when to do so would depart from the true intent of the legislature or would otherwise yield conclusions inconsistent with the purpose of the act. This Court has, in many cases involving the construction of statutes, cautioned against narrowly interpreting a statute as to defeat the purpose of the legislator, and rejected the literal interpretation of statutes if to do so would lead to unjust or absurd results.
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> Indeed, to leave undetermined the mode of appeal from the Secretary of Finance would be an injustice to taxpayers prejudiced by his adverse rulings. To remedy this situation, *We* imply from the purpose of RA 1125 and its amendatory laws that the CTA is the proper forum with which to institute the appeal. This is not, and should not, in any way, be taken as a derogation of the power of the Office of President but merely as recognition that matters calling for technical knowledge should be handled by the agency or quasi-judicial body with specialization over the controversy. As the specialized quasi-judicial agency mandated to adjudicate tax, customs, and assessment cases, there can be no other court of appellate jurisdiction that can decide the issues raised inthe CA petition, which involves the tax treatment of the shares of stocks sold. xxx"

It is noteworthy that in *Philam*, the Supreme Court categorically declared that the appellate court erred in holding that respondent's power to interpret tax laws is appealable directly to the CTA. Section 4 of the 1997 NIRC, as amended, readily provides that the Commissioner's power to interpret the provisions of this Code and other tax laws is subject to review by the Secretary of Finance.

In *Banco de Oro*, the Supreme Court said that "the determination of the validity of these issuances clearly falls within the exclusive appellate jurisdiction of the CTA under Section 7(1) of Republic Act No. 1125, as amended, subject to prior review by the Secretary of Finance, as required under Republic Act No. 8424."[5]

In the instant case, petitioners clearly failed to exhaust their administrative remedies for failure to elevate the case to the Secretary of Finance before resorting to this Court. Interestingly, petitioners' resort to this Court was triggered by the alleged February 16, 2024 press briefing by respondent, where respondent "effectively denied the plea of the said Industry Group's request and merely said that the RMC would be implemented on a 'case-to-case basis'"[6] Unfortunately, the same is not equivalent to an adverse ruling by the Secretary of Finance.

Meanwhile, the Court is aware of the more recent jurisprudential pronouncements of the Supreme Court, where it invoked its *jurisdictional prerogative* to rule on the validity of Bureau of Internal Revenue (BIR) despite failure of the taxpayer to elevate the case before the Secretary of Finance.

In *Bloomberry Resorts and Hotels, Inc. v. Bureau of Internal Revenue*,[7] the Supreme Court proclaimed that:

> From the foregoing jurisprudential pronouncements, it would appear that in questioning the validity of the subject revenue memorandum circular, petitioner should not have resorted directly before this Court considering that it appears to have failed to comply with the doctrine of exhaustion of administrative remedies and the rule on hierarchy of courts, a clear indication that the case was not yet ripe for judicial remedy. Notably, however, in addition to the justifiable grounds relied upon by petitioner for its immediate recourse (*i.e.* pure question of law, patently illegal act by the BIR, national interest, and prevention of multiplicity of suits), we intend to avail of our jurisdictional prerogative in order not to further delay the disposition of the issues at hand, and also to promote the vital interest of substantial justice. To add, in recent years, this Court has consistently acted on direct actions assailing the validity of various revenue regulations, revenue memorandum circulars, and the

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[5] *See* Note 1.
[6] Petition for Certiorari and/or Prohibition in CTA Case No. SCA-0018, Par. 25, Docket, p. 15.
[7] G.R. No. 212530, August 10, 2016.

likes, issued by the CIR. The position we now take is more in accord with latest jurisprudence. Upon the exercise of this prerogative, we are ushered into the merits of the case.

Consequently, in the most recent case of *Manila Peninsula Hotel, Inc. v. Commissioner of Internal Revenue*,[8] the Supreme Court also invoked its *jurisdictional prerogative* and reiterated its reasoning in *Bloomberry*, thus:

> "In the assailed Decision, the CTA EB upheld the validity of Revenue Memorandum Circular No. 46-2008 and BIR Ruling No. 99-2011 on the ground that Manila Peninsula failed to invoke the power of review of the Secretary of Finance.
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> The Court agrees with the CTA EB. The validity of Revenue Memorandum Circular No. 46-2008 and Revenue Memorandum Circular No. 31-2011 should have been first subjected to the review of the Secretary of Finance before Manila Peninsula sought judicial recourse with the CTA as dictated by the rule on exhaustion of administrative remedies.
>
> The doctrine of exhaustion of administrative remedies is not without practical and legal reasons. For one thing, availing of administrative remedies entails lesser expenses and provides for a speedier disposition of controversies. It is no less true to state that courts of justice, for reasons of comity and convenience, will shy away from a dispute until the system of administrative redress has been completed and complied with to give the administrative agency concerned every opportunity to correct its error and to dispose of the case. While there are recognized exceptions to this salutary rule, Manila Peninsula has failed to prove the presence of any of those in the instant case.
>
> Nevertheless, despite the failure of Manila Peninsula to file an appeal with the Secretary of Finance in assailing the validity of Revenue Memorandum Circular No. 46-2008 and Revenue Memorandum Circular No. 31-2011, the Court deems it prudent, if not crucial, to take cognizance of, and accordingly act on, the Petition as they assail the validity of the actions of the CIR that affect the taxation of services in the hotel industry and international airlines, as addressing it can have significant economic implications. For this reason, the Court, following recent jurisprudence, avails itself of its judicial prerogative in order not to delay the

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[8] G.R. No. 229338, April 17, 2024.

disposition of the case at hand and to promote the vital interest of justice. As the Court held in *Bloomberry Resorts and Hotels, Inc. v. BIR:*

> 'From the foregoing jurisprudential pronouncements, it would appear that in questioning the validity of the subject revenue memorandum circular, petitioner should not have resorted directly before this Court considering that it appears to have failed to comply with the doctrine of exhaustion of administrative remedies and the rule on hierarchy of courts, a clear indication that the case was not yet ripe for judicial remedy. **Notably, however, in addition to the justifiable grounds relied upon by petitioner for its immediate recourse (*i.e.*, pure question of law, patently illegal act by the BIR, national interest, and prevention of multiplicity of suits), we intend to avail of our jurisdictional prerogative in order not to further delay the disposition of the issues at hand, and also to promote the vital interest of substantial justice. To add, in recent years, this Court has consistently acted on direct actions assailing the validity of various revenue regulations, revenue memorandum circulars, and the likes, issued by the CIR. The position we now take is more in accord with latest jurisprudence**.'"

Petitioners anchor the instant Petition on the alleged imminent threat of the subject RMC to the Philippine economy, thus:

> "23. By reason of RMC No. 5-2024, there is a material, serious, and imminent threat to the continued and unhampered provision of these services which, as mentioned, are indispensable/integral/crucial to the operations of the Petitioners. There will also be an increase in costs of these services (i.e. 25% income tax and 12% VAT, considering the *gross up provision* it will effectively be 49%). As a result, Petitioners will be constrained to pass on these costs to their clients which will then ultimately have grave consequences to the Philippine businesses, and in general, to the Philippine economy"[9]

Meanwhile, respondent manifested in his Comment/Opposition that the issues raised by petitioners were already answered through the issuance of RMC No. 38-2024 on March 15, 2024. It provides:

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[9] Petition for Certiorari and/or Prohibition in CTA Case No. SCA-0018, Docket, p. 14.

REVENUE MEMORANDUM CIRCULAR NO. 38-2024

SUBJECT	:	*Clarifying the Issues Raised on Revenue Memorandum Circular No. 5-2024*
TO	:	*All Revenue Officers, Employees and Others Concerned*

This Circular is being issued to address and clarify the issues raised on Revenue Memorandum Circular (RMC) No. 5-2024.

Q1: Does the ruling in *Aces Philippines Cellular Satellite Corp. v. Commissioner of Internal Revenue*, finding that the source of income of the Satellite Air Time Purchase Agreement between *Aces Bermuda* and *Aces Philippines* to be within the Philippines and, thus, subject to income tax, automatically apply to international service provision or cross-border services agreements listed in Question No. 2 of RMC No. 5-2024?

A1. No. Question No. 2 of RMC No. 5-2024 listed international service provision or cross-border services (*e.g.*, Consulting Services, IT Consulting, Financial Services, etc.) only to highlight that — like *Aces Philippines* — these services are likewise performed, rendered, delivered, or supplied by a non-resident foreign corporation (NRFC) to a domestic/resident entity in the Philippines. There is nothing therein expressly stating that the decision in *Aces Philippines*, finding the source of income of the service agreement to be within the Philippines and, thus, subject to final withholding tax, automatically applies to the listed international service provision or cross-border services.

The determination on whether the source of income of the listed cross-border services is within the Philippines is found in Question No. 3 of RMC No. 5-2024 using the long-standing rule that, *the source of income is in the Philippines if the property, activity or service that produces the income is in the Philippines. The flow of wealth proceeded from, and occurred within the Philippine territory, enjoying the protection accorded by the Philippine government.*

The determination of the source of income involves an examination of all the components of the cross-border service agreement involving two tax jurisdictions (*i.e.*, residence of the NRFC and the Philippines), taking into account the services to be performed in its entirety, and not singled out or compartmentalized one particular activity as the income producing activity. This approach is aligned with the Civil Code provision that, there is performance when *'the thing or service in which the obligation consists has been completely delivered or rendered, as the case may be.'* Crucial factors to such determination are on whether the cross-border services are dependent on the successful use, consumption or utilization by the Philippine purchaser of the service for income to be accrued; or on whether the performance of the service depends on the facilities located in the Philippines; or on whether the particular stages occurring in the Philippines are so integral to the over-all transaction that the business activity would not have been accomplished without it; among others.

Q2: Do the principles laid down in RMC No. 5-2024 run counter to the rules on the source of income under Section 42 of the National Internal Revenue Code of 1997, as amended (Tax Code)?

A2: No. Question No. 3 of RMC No. 5-2024 clearly spelled out the main guideline in determining the source of income for cross-border services identified in Question No. 2 (Consulting Services, IT Outsourcing, Financial Services, etc.), and, that is, *'the source of income is in the Philippines if the property, activity or service that produces the income is in the Philippines. The flow of wealth proceeded from, and occurred within the Philippine territory, enjoying the protection accorded by the Philippine government.'*

Notably, the traditional rule on recognizing income under Section 42(A)(3) and (C)(3) of the National Internal Revenue Code of 1997, as amended (Tax Code), for labor or personal service is where the labor or service is performed. But in *Aces Philippines*, the Supreme Court held that, *'[i]n ascertaining the income source, We must inquire into the property, activity, or service that* ***produced the income, or where the inflow of wealth originated. It is insufficient to identify just any property or activity, or service. The subject may only be regarded as an income source if the particular property, activity or service causes an increase in economic benefits****, which may be in the form of an inflow or enhancement of assets or a decrease in liabilities with a corresponding increase in equity other than that attributable to a capital contribution.'*

Ultimately, therefore, following the above-pronouncement, the situs of the source of income for labor or personal service is not just the location but, more importantly, the location of the service **that produces the income or where the inflow of wealth originates**.

Q3: What is the meaning of the following statements in Question No. 7 of RMC 5-2024?

'Even if the services are conducted or paid abroad, but there are activities to be performed in the Philippines so essential that the entire service transaction cannot be accomplished without them, then, the benefits received theory applies. This means that the revenue-generating activity actually occurs within the Philippines. The income generated by the foreign company providing the services, which are considered sources within the Philippines, shall be subject to income tax and, consequently to final withholding tax.'

A3: The premise of such statements is that the service agreement occurs in multiple stages across different taxing jurisdictions, *i.e.*, jurisdiction of the NRFC and the Philippines. In such a situation, it is vitally important to examine all the components of the cross-border service agreement directly between the NRFC and the domestic/resident entity in the Philippines, looking at the services to be performed in its entirety, and not singled out or compartmentalized one particular activity as the income producing activity. Again, this approach is consistent with the Civil Code provision that, there is performance when *'the thing or service in which the obligation consists has been completely delivered or rendered.'* As stated in Question No. 3 of RMC 5-2024, *'in such instances,* ***it becomes imperative to ascertain whether the particular stages occurring in the Philippines are so integral to the overall transaction that the business activity would not have accomplished without them****. If the income-generating activities in the Philippines are deemed essential, the income derived from these activities would be considered as sourced from the Philippines for tax purposes, irrespective of where the payment is ultimately received. This principle aligns with the* ***benefits-received theory*** *in taxation, which submits that the jurisdiction providing the essential services or factors for income generation should be entitled to tax that income.'*

In the end, what applies in the aforesaid scenario is still the well-established rule that, *'[i]n ascertaining the income source, we must inquire into the property, activity, or service that* ***produced the income, or where the inflow of wealth originated,****'* highlighting that, *'****it is insufficient to identify just any property or activity, or service. The subject may only be regarded as an income source if the particular property, activity or service causes an increase in economic benefits*** *which may be in the form of an inflow or enhancement of assets or a decrease in* *liabilities with a corresponding increase in equity other than that attributable to a capital contribution.'*

Q4: Essentially, what is the benefits-received theory as reiterated and applied by the Supreme Court in *Aces Philippines* for purposes of determining the *situs* or place of taxation?

A4: In *Aces Philippines*, the Supreme Court held that, '. . . *where the inflow of wealth and/or economic benefits proceeds from, and occurs within the Philippine territory, it enjoys protection of the Philippine government. In consideration of such protection, the flow of wealth should share the burden of supporting the government, and thus, is subject to tax.'* This is essentially the benefits-received theory.

Q5: Are the rules enunciated in RMC No. 5-2024 inconsistent with the provisions of tax treaties?

A5. No. As propounded above, RMC No. 5-2024 merely set forth the guidelines to establish the source of taxation for cross-border services listed in Question No. 2 (Consulting Service, IT Outsourcing, Financial Services, etc.), which is, that *the source of taxation is the property, activity, or service that produces the income or where the inflow of wealth originates.*

Once the source of income is **established** to be within the Philippines using the aforesaid guidelines, then, the affected taxpayer can invoke the application of a particular tax treaty to assert that the income derived or sourced within the Philippines (*e.g.*, business profits, dividends, royalties or interests) is exempt from income tax for lack of permanent establishment or subject to preferential rate, as the case may be. In short, the application of the benefits of the tax treaty, such as tax exemption of business profits for lack of permanent establishment, presupposes that the *situs* of the source of income is in the Philippines.

Currently, the Philippines has forty-four (44) existing tax treaties with other tax jurisdictions.

The provisions, therefore, of RMC No. 5-2024 are not inconsistent with those of the tax treaties entered into by the Philippines.

Q6: If it is established that the source of income of cross-border services is within the Philippines applying the rule that the source of income is the location of the property, activity, or service that produces the income, will the subject transaction be also subject to VAT?

A6. Yes. Sections 105 and 108 of the Tax Code provide that services rendered or performed in the Philippines by non-resident foreign persons are subject to VAT.

Section 108 also subject non-resident foreign persons from VAT if their services involve, among others:

(a) the lease or the use of or the privilege to use any copyright, patent, design or model, plan, secret formula or process, goodwill, trademark, trade brand or other like property or right;

(b) the lease or the use of, the right to use of any industrial, commercial or scientific equipment;

(c) the supply of scientific, technical, industrial or commercial knowledge or information;

(d) the supply of technical advice, assistance or services rendered in connection with technical management or administration of any scientific, industrial or commercial undertaking, venture, project or scheme; among others.

Pursuant to Section 114(C) of the Tax Code, and as implemented by Section 4.114-2 of Revenue Regulations (RR) No 16-2005, as amended, the mode of VAT collection on payment for lease or use of property rights owned, and other services rendered in the Philippines, by non-resident foreign persons is thru withholding.

Q7: Why is Question No. 4 on reimbursable or allocable expenses for cross-border services between or among related parties also included in RMC No. 5-2024?

A7: RMC No. 5-2024 further clarifies the proper tax treatment of cross-border services in light of the *Aces Philippines* decision. Cross-border services usually involve related parties, common of which are intra-group services, like management, financial and administrative services; technical and support services; purchasing, marketing and distribution services; and other commercial services provided in connection with the nature of the group's business. As these are intra-group services, issues, such as on whether their pricing of such services is arm's length, may arise. As such, it is deemed necessary to also lay down the basic rules on reimbursable or allocable expenses for services between or among related parties to have a wholistic approach insofar as the determination of the proper tax treatment of cross-border services is concerned.

Like any other cross-border service agreement, the <u>source of income is not determined by where income is disbursed or physically received</u> but rather where the business activity that produced such income is actually conducted. The determination of the source of income for the charges made by the parent entity or affiliates to a related local company for the services made by the former to the latter is still the time-honored rule, as reiterated by the Supreme Court in *Aces Philippines*, that, *'in ascertaining the income source, we must inquire into the property, activity, or service that produced the income, or where the inflow of wealth originated,"* putting emphasis that, *"the subject may only be regarded as an income source if the particular property, activity or service causes an* ***increase in economic benefits****, which may be in the form of an inflow or enhancement of assets or a decrease in liabilities with a corresponding increase in equity other than that attributable to a capital contribution.'*

Q8: Is the 25% final withholding on gross income received by non-resident foreign person from all <u>sources</u> within the Philippines, including the 12% final withholding VAT on payment for lease or use of properties rights owned, and other services rendered in the Philippines, by non-resident foreign person, a new imposition?

A8: No. The 25% final withbolding on gross income received by non-resident foreign person from all **<u>sources</u>** within the Philippines is clearly provided for in Sections 25(B) and 28(B) of the Tax Code. On the other hand, the 12% final withholding VAT on payment for lease or use of property rights owned, and other services rendered in the Philippines, by non-resident foreign person is pursuant to Sections 105, 108 and 114(C) of the Tax Code, and as implemented by Section 4.114-2 of RR No. 16-2005, as amended.

All internal revenue officers, employees and others concerned are hereby enjoined to give this Circular the widest dissemination and publicity as possible.

This Circular shall take effect immediately.

(SGD.) ROMEO D. LUMAGUI, JR.
Commissioner of Internal Revenue

Based on RMC No. 38-2024, the taxability of the enumerated entities, including petitioners, depends on the source of taxation and existing tax treaties.

In other words, at this point, it is not clear whether RMC No. 5-2024 has significant adverse effects to petitioners or to the national economy, in general, for the Court to adopt the principle of *jurisdictional prerogative.* Presently, the Court is confronted by adverse assumptions of petitioners. However, the Court is not prepared to draw conclusions from mere assumptions.

The filing of the subject Petitions for Certiorari and/or Prohibition is premature

Finally, based on the above discussions, the Court finds that the instant Petitions are premature.

Sections 1 and 2, Rule 65 of the Revised ROC respectively provide:

> "**Section 1.** *Petition for certiorari.* — When any tribunal, board or officer exercising judicial or quasi-judicial functions has acted without or in excess its or his jurisdiction, or with grave abuse of discretion amounting to lack or excess of jurisdiction, and **there is no appeal, or any plain, speedy, and adequate remedy in the ordinary course of law**, a **person aggrieved** thereby may file a verified petition in the proper court, alleging the facts with certainty and praying that judgment be rendered annulling or modifying the proceedings of such tribunal, board or officer, and granting such incidental reliefs as law and justice may require.
>
> The petition shall be accompanied by a certified true copy of the judgment, order or resolution subject thereof, copies of all pleadings and documents relevant and pertinent thereto, and a sworn certification of non-forum shopping as provided in the third paragraph of section 3, Rule 46." *(Emphasis supplied)*
>
> "**Section 2.** *Petition for prohibition.* — When the proceedings of any tribunal, corporation, board, officer or person, whether exercising judicial, quasi-judicial or ministerial functions, are without or in excess of its or his jurisdiction, or with grave abuse of discretion amounting to lack or excess of jurisdiction, **and there is no appeal or any**

> **other plain, speedy, and adequate remedy in the ordinary course of law**, a **person aggrieved** thereby may file a verified petition in the proper court, alleging the facts with certainty and praying that judgment be rendered commanding the respondent to desist from further proceedings in the action or matter specified therein, or otherwise granting such incidental reliefs as law and justice may require.
>
> The petition shall likewise be accompanied by a certified true copy of the judgment, order or resolution subject thereof, copies of all pleadings and documents relevant and pertinent thereto, and a sworn certification of non-forum shopping as provided in the third paragraph of section 3, Rule 46." *(Emphasis supplied)*

As previously discussed, the remedy of elevating the case before the Secretary of Finance under Section 4 of the 1997 NIRC, as amended, was available prior to resorting to this Court. Hence, petitioners had a plain, speedy and adequate remedy in the ordinary course of law which they failed to avail.

In addition, it remains to be seen whether petitioners could be adversely affected by RMC No. 5-2024, considering that the imminent threat alleged in their respective petitions is arguably a threat based on mere assumptions. Without necessarily delving into its propriety, this assumed threat was seemingly addressed in the subsequent RMC No. 38-2024. Hence, it remains to be seen whether petitioners could be considered as "*persons aggrieved*" within the contemplation of Sections 1 and 2, Rule 65 of the Revised ROC.

Considering the foregoing, the Court finds that the dismissal of the instant Petitions is in order.

FOR THESE REASONS, the Petition for Certiorari and/or Prohibition in CTA Case Nos. SCA-0018 and SCA-0020, respectively, are **DISMISSED**, for lack of jurisdiction. Meanwhile, petitioners' Application for a Temporary Restraining Order and/or Writ of Preliminary Injunction and Issuance of Confidentiality Order are deemed **MOOT** and **ACADEMIC**.

SO ORDERED.

Catherine T. Manahan

CATHERINE T. MANAHAN
Associate Justice

Marian Ivy F Reyes - Fajardo
(With Separate Opinion)
MARIAN IVY F. REYES-FAJARDO
Associate Justice

HENRY S. ANGELES
Associate Justice

REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

THIRD DIVISION

AUSTRALIA AND NEW ZEALAND BANKING GROUP LIMITED, PHILIPPINES BRANCH, ET AL.,
Petitioners,

CTA SCA No. 0018

\- versus -

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

x - x

BANCNET INCORPORATED,
Petitioner,

CTA SCA No. 0020

Members:

MANAHAN, *Chairperson,*
REYES-FAJARDO, and
ANGELES, *JJ.*

\- versus -

Promulgated:

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

NOV 1 1 2024
3:24 p.m.

x - x

SEPARATE OPINION

REYES-FAJARDO, *J.*:

I agree in the result. I, however, pose a different view on one of the reasons for the dismissal of CTA SCA Case Nos. 0018 and 0020.

CTA SCA Case Nos. 0018 and 0020 were both commenced by Petitions for Certiorari and/or Prohibition with Application for a Temporary Restraining Order and/or Writ of Preliminary Injunction and Issuance of Confidentiality Order. These petitions seek to nullify Revenue Memorandum Circular (RMC) Nos. 5-2024 and 38-2024, both issued by the Commissioner of Internal Revenue (CIR), for being allegedly offensive of the law and constitution.

Among the justifications for the dismissal thereof is that since petitioners failed to first elevate RMC Nos. 5-2024 and 38-2024 for review of the Secretary of Finance, as enjoined by Section 4 of the 1997 National Internal Revenue Code (NIRC), as amended, they violated the doctrine of prior exhaustion of administrative remedies. Such violation in turn resulted in the Court of Tax Appeals (CTA)'s lack of jurisdiction over CTA SCA Nos. 0018 and 0020.

I offer a different take on the consequence of such violation.

Specifically, petitioners' failure to first bring RMC Nos. 5-2024 and 38-2024 for review of the Secretary of Finance, before resorting to court action, as recognized in Section 4 of the NIRC, as amended, is indeed violative of the principle of prior exhaustion of administrative remedies. Yet, the non-adherence with said principle would *not* lead to the CTA's lack of jurisdiction over the subject matter of CTA SCA Nos. 0018 and 0020. The adverse effect thereof is that petitioners would have no cause of action before the CTA, resulting in the dismissal of their Petitions. *Oceanagold (Philippines), Inc. v. Commissioner of Internal Revenue*[1] is on point:

> "Under the doctrine of exhaustion of administrative remedies, recourse through court action cannot prosper until after all such administrative remedies have first been exhausted. If remedy is available within the administrative machinery, this should be resorted to before resort can be made to courts. It is settled that **non-observance of the doctrine of exhaustion of administrative remedies results in lack of cause of action, which is one of the grounds in the Rules of Court justifying the dismissal of the complaint.**"[2]

1 G.R. No. 234614, June 14, 2023, citing *Commissioner of Internal Revenue v. Court of Tax Appeals (First Division),* G.R. Nos. 210501, 211294 & 212490, March 15, 2021.

2 Boldfacing supplied.

All said, I **CONCUR** in the dismissal of CTA SCA Nos. 0018 and 0020, *solely* on the ground of prematurity, as discussed in pages 20-21 of the *ponencia*.

Marian Ivy F. Reyes-Fajardo
MARIAN IVY F. REYES-FAJARDO
Associate Justice