REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

EN BANC

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COMMISSIONER OF INTERNAL REVENUE, Petitioner,	**CTA EB No. 1788** (CTA Case No. 9088)
	Present:
- versus -	**DEL ROSARIO,** *P.J.*, **CASTAÑEDA, JR., UY, FABON-VICTORINO, MINDARO-GRULLA, RINGPIS-LIBAN, MANAHAN, BACORRO-VILLENA,** and **MODESTO-SAN PEDRO,** *JJ.*
SPOUSES MICHAEL GAVIN RICHARD L. DE LOS REYES AND JENNIFER C. CO-DE LOS REYES, Respondents.	***Promulgated:*** OCT 03 2019 2:28 p.m.

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DECISION

UY, *J.*:

The instant *Petition for Review* filed on March 7, 2018[1] by the Commissioner of Internal Revenue against Spouses Michael Gavin Richard L. De Los Reyes and Jennifer C. Co-De Los Reyes, seeks to reverse the Decision dated October 19, 2017[2] and Resolution dated February 1, 2018[3], both promulgated by the Third Division of this Court in CTA Case No. 9088, entitled *"Spouses Michael Gavin Richard L. De Los Reyes and Jennifer C. Co-De Los Reyes, Petitioners, versus Commissioner of Internal Revenue, Respondent,"* the dispositive portions of which respectively read as follows:

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[1] EB Docket, pp. 6 to 13.

[2] Penned by Associate Justice Lovell R. Bautista (now retired), and concurred by Associate Justices Esperanza R. Fabon-Victorino, and Ma. Belen M. Ringpis-Liban, EB Docket, pp. 15 to 30.

[3] *Supra*, EB Docket, pp. 32 to 35.

Decision dated October 19, 2017:

"**WHEREFORE,** premises considered, the instant Petition for Review is hereby **GRANTED**. Respondent Commissioner of Internal Revenue is hereby **ORDERED** to refund in favor of petitioners Spouses Michael Gavin Richard L. de los Reyes and Jennifer C. Co-de los Reyes the amount of **One Million Nine Hundred Forty-Eight Thousand Eight Hundred Thirty-Two and 34/100 Pesos (Php1,948,832.34)**, representing petitioners' erroneously and illegally collected income tax on compensation income from the Asian Development Bank for calendar year 2012.

SO ORDERED."

Resolution dated February 1, 2018:

"**WHEREFORE,** premises considered, respondent's Motion for Reconsideration (Decision of 19 October 2017) is hereby **DENIED** for lack of merit. The Decision promulgated on October 19, 2017 is **AFFIRMED.**

SO ORDERED."

THE FACTS

Petitioner is the duly appointed Commissioner of the Bureau of Internal Revenue who is empowered by law to act on claims for refund or credit, with office address at the Bureau of Internal Revenue National Office Building, Diliman, Quezon City.

Respondents, Spouses Michael Gavin Richard L. de los Reyes and Jennifer C. Co-de los Reyes, are Filipinos, of legal age, and with address at 6 ADB Avenue, Mandaluyong City.

For calendar year (CY) 2012, respondents were employed by the Asian Development Bank (ADB). Respondent Michael L. de los Reyes was a member of ADB's Treasury Department (Treasury Client Solutions Unit), while respondent Jennifer C. Co-de los Reyes was a member of ADB's Budget, Personnel, and Management Systems Department (HR Policy and Program Division).

On April 12, 2013, petitioner issued Revenue Memorandum Circular (RMC) No. 31-2013, entitled *"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."* Under Section 2(d)(1) of the administrative issuance, petitioner stated that only officers and staff of the ADB who are not Philippine nationals are exempt from income tax.

On July 12, 2013, respondents filed their joint Annual Income Tax Return for CY 2012 and paid ₱1,948,832.34 pursuant to RMC No. 31-2013. The amount paid can be broken down, as follows:

	Gross Compensation Income	***Taxable Income***	***Income Tax Due***
MICHAEL DE LOS REYES	₱4,880,589.63	₱4,780,589.63	₱1,494,788.68
JENNIFER CO-DE LOS REYES	₱1,608,261.42	₱1,528,261.42	₱ 454,043.65
		AGGREGATE TAX PAYABLE	**₱1,948,832.34**

Thereafter, on July 10, 2015, respondents filed a letter-request for the refund of their alleged erroneously and illegally collected income tax for CY 2012.

Due to petitioner's inaction on respondents' letter-request, respondents filed a *Petition for Review* before the Court in Division on July 13, 2015. The case was docketed as CTA Case No. 9088.

In the *Petition for Review* of respondents, the latter invoked the ruling of the Mandaluyong City Regional Trial Court (RTC) – Branch 213, in Civil Case No. MC14-8775, entitled *"Erwin Salavera and Portia Gonzales versus Commissioner of Internal Revenue"* ("*Salavera* case"), to the effect that Section 2(d)(1) of RMC No. 31-2013 is void for being issued without legal basis, in excess of authority and/or without due process of law.

On September 28, 2015, petitioner filed his *Answer*, alleging, among others, that: 1) the Mandaluyong City RTC – Branch 213, has no jurisdiction over the case filed by the employees of the ADB, pertaining to the validity of RMC No. 31-2013; 2) granting without admitting that RTC Branch 213 has jurisdiction to rule on the validity of RMC No. 31-2013, its decision has yet to become final as the case was appealed to the Court of Appeals; 3) respondents are resident

Filipino citizens and are subject to Philippine income tax; 4) taxation of income in the Philippines is based on citizenship, residency, and the source principles; 5) in signing the ADB Headquarters Agreements 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 made a clear limitation insofar as its right to tax its nationals; 6) RMC No. 31-2013 is only a clarification of existing policies already in Philippine law; 7) the exception under RMC No. 31-2013 is still subject to the power of the government to tax its nationals; 8) the respondents must prove their compliance with the documentary and legal requirements as provided under Section 229 of the National Internal Revenue Code (NIRC) of 1997, as amended; 9) tax exemptions are never presumed and are strictly construed against the taxpayer and liberally in favor of the taxing authority; and 10) a tax refund is in the nature of a tax exemption, which must be construed in *strictissimi juris* against the taxpayer.

After the pre-trial conference held on February 16, 2016, the parties filed their *Joint Stipulation of Facts and Issues* on March 11, 2016, which was adopted by the Court in Division in the Pre-Trial Order issued on April 6, 2016.

During trial, respondents presented the following witnesses: (1) Michael Gavin Richard L. de los Reyes, and (2) Jennifer C. Co-de los Reyes. Thereafter, respondents filed on August 9, 2016, their *Formal Offer of Documentary Exhibits*. No comment was filed thereto by petitioner. On September 8, 2016, the Court resolved to admit all of respondents' Exhibits ("P-1", "P-1-a", "P-1-b", "P-2", "P-2-a", "P-3", "P-3-a", "P-4", "P-5", "P-6", "P-7", "P-8", "P-9", "P-9-a", "P-10", and "P-10-a").

For his part, petitioner manifested that he would not be presenting evidence in CTA Case No. 9088. As directed by the Court in Division, respondents filed their *Memorandum* by registered mail on November 23, 2011; while petitioner filed a *Manifestation* on December 22, 2016, stating that he was adopting the arguments raised in his *Answer* as his memorandum.

In the Resolution dated January 6, 2017, the Court in Division submitted CTA Case No. 9088 for decision.

In the assailed Decision dated October 19, 2017,[4] the Court in Division granted respondents' *Petition for Review*, and petitioner was ordered to refund respondents the amount of ₱1,948,832.34, representing petitioners' erroneously and illegally collected income tax on compensation income from the ADB for CY 2012.

Petitioner then filed his *Motion for Reconsideration (Decision of 19 October 2017)* on November 10, 2017,[5] to which respondents filed their *Comment (Re: Motion for Reconsideration dated 09 November 2017)* on December 27, 2017.[6] In the assailed Resolution dated February 1, 2018,[7] the Court in Division denied petitioner's *Motion for Reconsideration (Decision of 19 October 2017)* for lack of merit.

Undaunted, petitioner filed a *Motion for Extension of Time to File Petition for Review En Banc* on February 20, 2018.[8] In the Resolution dated February 22, 2018,[9] petitioner was granted a final and non-extendible period of fifteen (15) days from February 20, 2018, or until March 7, 2018, within which to file his *Petition for Review*.

Thereafter, petitioner filed the instant *Petition for Review* on March 7, 2018.[10]

In the Resolution dated March 27, 2018,[11] petitioner was given a period of five (5) days within which to submit his *Affidavit of Service*. Pursuant thereto, petitioner filed his *Compliance* on April 16, 2018.[12] In the Resolution dated May 7, 2018,[13] this Court noted that the said *Compliance* was filed beyond the date required in this Court's Resolution; however, the same was admitted in the interest of substantial justice.

Subsequently, respondents were ordered to file their *Comment* within ten (10) days from notice.[14] Thus, respondents filed their

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[4] EB Docket, pp. 15 to 30; Division Docket (CTA Case No. 9088) – Vol. 2, pp. 649 to 664.
[5] Division Docket (CTA Case No. 9088) – Vol. 2, pp. 666 to 671.
[6] Division Docket (CTA Case No. 9088) – Vol. 2, pp. 675 to 684.
[7] EB Docket, pp. 32 to 35; Division Docket (CTA Case No. 9088) – Vol. 2, pp. 689 to 692.
[8] EB Docket, pp. 1 to 4.
[9] EB Docket, p. 5.
[10] EB Docket, pp. 6 to 13.
[11] EB Docket, pp. 40 to 42.
[12] EB Docket, pp. 43 to 45.
[13] EB Docket, pp. 47 to 48.
[14] Resolution dated May 7, 2018, EB Docket, pp. 47 to 48.

Comment (Re: Petition for Review dated 06 March 2018) on May 31, 2018.[15]

On July 6, 2018, the Court resolved to give due course to the *Petition for Review*, and gave the parties a period of thirty (30) days to file their respective memoranda.[16] Respondents filed their *Memorandum* on September 10, 2018.[17] Petitioner, however, failed to file his memorandum despite due notice.[18] In the Resolution dated October 4, 2018,[19] the instant case was deemed submitted for decision.

Hence, this Decision.

ASSIGNMENT OF ERRORS

Petitioner raises, in his *Petition for Review*, the following assignment of errors supposedly committed by the Court in Division, to wit:

> "I. The Honorable Court erred in granting the Petition for Review and ordering the refund of **One Million Nine Hundred Forty-Eight Thousand Eight Hundred Thirty-Two and 34/100 Pesos (Php1,948,832.34)** in favor of [respondents] Spouses Michael Gavin Richard L. Delos Reyes and Jennifer C. Co-Delos Reyes.
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> II. The Honorable Court erred when it anchored on the retroactive application of RMC 31-2013 in the taxation of salaries and emoluments paid by ADB to its officers and employees who are resident citizens."[20]

Petitioner's arguments:

Petitioner contends that taxation of salaries and emoluments paid by ADB to its officers and employees who are resident citizens, is not anchored on the retroactive application of RMC No. 31-2013.

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[15] EB Docket, pp. 49 to 59.
[16] Resolution dated July 6, 2018, EB Docket, pp. 64 to 65.
[17] EB Docket, pp. 66 to 85.
[18] Records Verification dated September 19, 2018 issued by the Judicial Records Division of this Court, EB Docket, p. 89.
[19] EB Docket, pp. 91 to 92.
[20] EB Docket, p. 9.

According to petitioner, the taxability of the income of the ADB Filipino employees is not dependent on the validity or invalidity of RMC No. 31-2013; rather, their taxability is based on the existing provisions of the NIRC of 1997, as amended, in relation to the treaty and/or agreement between the Philippine government and the ADB. Thus, the reckoning point of the taxability of their income is the taxable year that they were employed by the ADB.

Respondents' counter-arguments:

Respondents counter-argue that they are entitled to a refund of the income tax paid to/collected by the Bureau of Internal Revenue (BIR) on compensation income they received from the ADB for taxable year 2012.

Allegedly, ADB employees are exempt from income tax under the ADB charter. Moreover, 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.

In addition, respondents argue that they have duly complied with the requisites of Section 229 of the Tax Code, granting the refund of the amount of ₱1,948,832.34, which was erroneously paid by the respondents to the BIR.

Finally, assuming that RMC No. 31-2013 is valid, respondents submit that laws shall have no retroactive effect, unless the contrary is provided; and rules and regulations on taxation should not be given retroactive application if it will be prejudicial to the taxpayer.

THE COURT *EN BANC*'S RULING

The instant *Petition for Review* has merit.

The NIRC of 1997, as amended, provides for the imposition of income tax on compensation income earned by resident Filipino citizens; not RMC No. 31-2013.

Petitioner argues that the taxation of the income received by resident Filipino employees of the ADB, is not anchored on the retroactive application of RMC No. 31-2013. Instead, the taxability of the said income is based on the existing provisions of the NIRC of 1997, as amended.

We agree with petitioner.

In this case, the imposition of income tax on the employees of ADB, who are resident Filipino citizens or nationals, are anchored on the pertinent provisions of the NIRC of 1997, as amended.

As provided for in Section 23(A) of the NIRC of 1997, the income of a resident Filipino citizen, whether derived from sources within or without the Philippines, are subject to tax, 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 or without the Philippines**;" *(Emphasis supplied)*

In addition and in relation thereto, Sections 24, 31 and 32(A)(1) of the NIRC of 1997, as amended by Republic Act No. 9504[21] (the law in effect for CY 2012), read:

> "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 <u>by every individual citizen of the Philippines</u> residing therein**;

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[21] AN ACT AMENDED SECTIONS 22, 24, 34, 35, 51, AND 79 OF REPUBLIC ACT NO. 8424, AS AMENDED, OTHERWISE KNOWN AS THE NATIONAL INTERNAL REVENUE CODE OF 1997.

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(2) *Rates of Tax on Taxable Income of Individuals.* – **The tax shall be computed in accordance with and at the rates established in the following schedule:**

Not over ₱10,000..............................	5%
Over ₱10,000 but not over ₱30,000......	₱500+10% of the excess over ₱10,000
Over ₱30,000 but not over ₱70,000......	₱2,500+15% of the excess over ₱30,000
Over ₱70,000 but not over ₱140,000.....	₱8,500+20% of the excess over ₱70,000
Over ₱140,000 but not over ₱250,000...	₱22,500+25% of the excess over ₱140,000
Over ₱250,000 but not over ₱500,000...	₱50,000+30% of the excess over ₱250,000
Over ₱500,000................................	₱125,000+32% of the excess over ₱500,000

xxx xxx xxx." *(Emphases and underscoring supplied)*

"SEC. 31. *Taxable Income Defined.* — **The term 'taxable income' means the pertinent items of gross income specified in this Code**, less the deductions and/or personal and additional exemptions, if any, authorized for such types of income by this Code or other special laws." *(Emphasis supplied)*

"SEC. 32. *Gross Income.* –

(A) *General Definition.* – Except when otherwise provided in this Title, **gross income means all income derived from whatever source, including (but not**

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limited to) the following items:

(1) **Compensation for services in whatever form paid, including, but not limited to** fees, **salaries, wages**, commissions, and similar items;" *(Emphases supplied)*

Based on the foregoing provisions, it is apparent that the compensation income of a citizen or national of the Philippines, who is residing therein, from all sources within and without the Philippines, is subject to income tax.

Correspondingly, considering that respondents are Filipinos and resident of the Philippines,[22] they are subject to income tax, pursuant to Sections 23(A) and 24(A)(1), in relation to Sections 31 and 32(A)(1), all of the NIRC of 1997, as amended.

ADB employees, who are nationals or citizens of the Philippines, are not exempt from income tax.

Respondents argue that under the ADB Charter, ADB employees are exempt from income tax.

We partly agree.

Without doubt, Article 56 of the ADB Charter[23], to which the Philippines is a signatory, provides, in part, as follows:

"Article 56

EXEMPTION FROM TAXATION

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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

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[22] Par. 1.1, *Joint Stipulation of Facts and Issues*, Division Docket (CTA Case No. 9088) – Vol. 1, p. 227.
[23] Formally known as the *"AGREEMENT ESTABLISHING THE ASIAN DEVELOPMENT BANK"*.

> 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." *(Emphasis supplied)*

Having the foregoing provisions as a sole basis, it can be said that the salaries and emoluments paid by the ADB to its directors, alternates, officers or employees, including experts performing missions for ADB, are exempt from income tax. However, the above-stated ADB Charter is not the only Agreement that the Philippine Government has entered into, insofar as the taxation of the said salaries and emoluments paid by the ADB is concerned.

On December 22, 1966, the Philippine Government has likewise entered into, with the ADB, the *"Agreement Between the Asian Development Bank and the Government of the Republic of the Philippines Regarding the Headquarters of the Asian Development Bank"* (RP-ADB Agreement) — which should be equally binding, and be given force and effect, as that of the ADB Charter.

Section 45(b) of the RP-ADB Agreement reads as follows:

> "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**:
>
> xxx xxx xxx
>
> (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>**;" *(Emphases and underscoring supplied)*

Based on the foregoing provisions, while it may be true that officers and staff of the ADB are granted exemption from taxation with respect to salaries and emoluments paid by the said Bank under the RP-ADB Agreement, the same is subject to the qualification that the Philippine Government may exercise its power to tax over ADB officers and employees, who are citizens or nationals of the Philippines.

In this connection, it must be emphasized that through the earlier quoted Sections 23(A), 24(A)(1), 31, and 32(A)(1) of the NIRC of 1997, as amended, the Philippine Government had clearly exercised its power to tax its national or citizens.

To be clear, while in general, the salaries and emoluments of officers and staff of the ADB are exempt from income tax, such exemption does not extend to ADB officers and staff who are Philippine citizens or nationals. Such being the case, being Philippine citizens or nationals, respondents' salaries and emoluments are subject to income tax, pursuant to Sections 23(A), 24(A)(1), 31, and 32(A)(1), of the NIRC of 1997, as amended.

The Mandaluyong City RTC – Branch 213, is without jurisdiction to declare Section 2(d)(1) of RMC No. 31-2013 as void. In any event, such declaration is erroneous.

To justify their supposed income tax exemption, respondents also invoke the *Salavera* case (decided by the Mandaluyong City RTC – Branch 213, in Civil Case No. MC14-8775), wherein Section 2(d)(1) of RMC No. 31-2013 was declared void for being issued without legal basis, in excess of authority and/or without due process of law.

We are not swayed.

In *Banco De Oro, et al. vs. Rizal Commercial Banking Corporation, et al.*,[24] the Supreme Court held:

> "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.
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> This Court, however, declares that **the Court of Tax Appeals may likewise take cognizance of cases**

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

directly challenging the constitutionality or validity of a tax law or regulation or administrative issuance (revenue orders, <u>revenue memorandum circulars</u>, 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.

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.

Republic Act No. 9282, a special and later law than Batas Pambansa Blg. 129 <u>provides an exception to the original jurisdiction of the Regional Trial Courts over actions questioning the constitutionality or validity of tax laws or regulations</u>. 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, <u>revenue memorandum circulars</u>, 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.**" *(Emphases and underscoring supplied)*

Based on the foregoing, the determination of the validity of administrative issuances issued by the BIR or petitioner, such as RMC No. 31-2013, falls within the *exclusive appellate jurisdiction* of this Court, not the RTC. Thus, the Mandaluyong City RTC – Branch 213, is not vested with jurisdiction to declare the invalidity of RMC No. 31-2013.

Needless to state, a judgement rendered by a court without jurisdiction is null and void and may be attacked anytime. It creates no rights and produces no effect. It remains a basic fact in law that the choice of the proper forum is crucial, as the decision of a court or tribunal without jurisdiction is a total nullity. A void judgment for want of jurisdiction is no judgment at all. All acts performed pursuant to it and all claims emanating from it have no legal effect.[25] Simply put, a void judgment or order has no legal and binding effect. It does not divest rights and no rights can obtained under it; all proceedings founded upon a void judgment are equally worthless.[26]

Correspondingly, the ruling of Mandaluyong City RTC – Branch 213, to the effect that Section 2(d)(1) of RMC No. 31-2013 is void, is a nullity. It did not have any legal and binding effect. Thus, it did not divest rights, and no rights can be obtained thereunder.

However, even assuming *arguendo* that RMC No. 31-2013 can be declared as invalid by the Mandaluyong City RTC, such declaration is erroneous.

For easy reference, We reproduce herein pertinent portions of RMC No. 31-2013, including Section 2(d)(1) thereof, *viz*:

> "SECTION 1. BACKGROUND.—
>
> xxx xxx xxx
>
> Section 23 of the National Internal Revenue Code (Tax Code) lays down the general principles in the taxation of citizens and alien individuals, to wit:

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[25] *Bilag, et al. vs. Ay-ay, et al.*, G.R. No. 189950, April 24, 2017.
[26] *Go vs. Echavez*, G.R. No. 174542, August 3, 2015.

> 'SECTION 23. General Principles of Income Taxation in the Philippines.—
>
> (A) A citizen of the Philippines residing therein is taxable on all income derived from sources within and without the Philippines;
>
> xxx xxx xxx
>
> (D) An alien individual, whether a resident or not of the Philippines, is taxable only on income derived from sources within the Philippines; xxx'

As an exemption to the general rule, it is noted that most international agreements which grant withholding tax immunity to foreign governments/embassies/ diplomatic missions and international organizations also provide exemption to their officials and employees who are foreign nationals and/or non-Philippine residents from paying income taxes on their salaries and other emoluments.

The tax consequence of compensation income received by those employed by foreign governments/ embassies/diplomatic missions situated in the Philippine hinges on the provisions of the duly recognized international agreements or local laws granting tax privileges to employees of said institutions. **It bears to emphasize that the exemption should only cover those individuals who were expressly and unequivocally identified in said international agreements or laws. Those not covered shall be subject to the general rule on taxability of Philippine nationals and alien individuals. Thus with respect to those not exempted by the provisions of applicable international agreements or laws, although their compensation income is exempt from withholding tax under the international agreements or the Withholding Tax Regulations, they are not relieved of their duty to report their compensation income to the Bureau and pay the taxes due thereon pursuant to Section 24 of the National Internal Revenue Code of 1997, as amended** ('Tax Code').

This Circular is being issued to evoke compliance by Philippine nationals and individual aliens who are liable to Philippine income tax under the provisions of the Tax Code and who were not given exemption under the terms of duly recognized international agreements or other Philippine laws.

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**:

xxx xxx xxx

(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

xxx xxx xxx

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:

xxx xxx xxx

(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**</u>

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its nationals;" Underscoring supplied

From the above, **only officers and staff of the ADB who are not Philippine nationals shall be exempt from Philippine income tax.**" *(Emphases supplied)*

A careful reading of the foregoing would reveal that petitioner merely exercised his power to interpret the pertinent provisions of the NIRC of 1997 in relation to the RP-ADB Agreement. Specifically, based on the cited provisions, petitioner, in effect, concluded that while the RP-ADB Agreement grants income taxation on the salaries and emoluments of officers and staff of ADB, as well as to experts and consultants performing missions therefor, such income taxation does not extend to ADB's officers and staff, who are Philippine nationals.

As already shown, the foregoing interpretation by petitioner is in accordance with Sections 23(A), 24(A)(1), 31, and 32(A)(1), of the NIRC of 1997, as amended. Thus, it was error for the Mandaluyong City RTC – Branch 213 to declare that Section 2(d)(1) of RMC No. 31-2013 is void. As a corollary, in view of the said provisions of law, even without the said Section 2(d)(1) of RMC No. 31-2013, the taxability of the salaries and emoluments of ADB officers and employees, who are Philippine citizens or nationals, remains.

Section 246 of the NIRC of 1997 is not applicable to the instant case.

Respondents further contends that granting, without admitting that RMC No. 31-2013 is valid, rules and regulations on taxation should not be given retroactive application if it will be prejudicial to the taxpayer, pursuant to Section 246 of the NIRC of 1997.

We are not convinced.

As already stated, in view of Sections 23(A), 24(A)(1), 31, and 32(A)(1), of the NIRC of 1997, as amended, the taxability of the salaries and emoluments of ADB officers and employees, who are Philippine citizens or nationals, remains, even without the said Section 2(d)(1) of RMC No. 31-2013. Thus, the said administrative issuance is not being given a retroactive application, since it is merely echoing what the law has already established.

But even granting that RMC No. 31-2013 is being given a retroactive application, such treatment is of no moment, and respondents cannot validly invoke Section 246 of the NIRC of 1997.

For easy reference, Section 246 of the NIRC of 1997 reads:

> "SEC. 246. *Non-Retroactivity of Rulings.* – **<u>Any revocation, modification or reversal</u> of any of the rules and regulations promulgated in accordance with the preceding Sections or any of the rulings or circulars promulgated by the Commissioner shall not be given retroactive application <u>if the revocation, modification or reversal</u> will be prejudicial to the taxpayers**, except in the following cases:
>
> (a) Where the taxpayer deliberately misstates or omits material facts from his return or any document required of him by the Bureau of Internal Revenue;
>
> (b) Where the facts subsequently gathered by the Bureau of Internal Revenue are materially different from the facts on which the ruling is based; or
>
> (c) Where the taxpayer acted in bad faith." *(Emphases and underscoring supplied)*

Based on the foregoing provision, it is a general rule that any revocation, modification, or reversal of any rules and regulations, ruling or circulars promulgated by petitioner, shall not have a retroactive application, if such revocation, modification or reversal will be prejudicial to the taxpayers. Thus, for the non-retroactive application rule under Section 246 of the NIRC of 1997 to apply, there must be certain rules and regulations, ruling or circular promulgated by petitioner that are being revoked, modified, or reversed.

In this case, however, there is no indication that any rules and regulations, rulings or circulars promulgated by petitioner, are being revoked, modified, or reversed by RMC No. 31-2013. Correspondingly, the rule against retroactive application under Section 246 of the NIRC of 1997 may not be applied in this case.

Respondents are not entitled to the refund of income taxes they paid for CY 2012.

Section 229 of the NIRC of 1997 provides as follows:

> "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 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 cause 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."

Based on the foregoing provision, the recovery of erroneously or illegally collected taxes is allowed. An *"erroneous or illegal tax"* is defined as one levied without statutory authority,[27] or upon property not subject to taxation or by some officer having no authority to levy the tax, or one which is some other similar respect is illegal.[28] In other words, for taxes to be refunded, it must be shown to have been erroneously or illegally collected.

In this case, however, respondents failed to establish the factual basis of their claim for a refund. Specifically, there is no showing that they fall within the coverage of those entitled to tax exemption under Section 45(b) of the RP-ADB Agreement. Thus, respondents are not entitled to the refund of income tax collected from them for CY 2012.

Tax refunds, like tax exemptions, are construed strictly against the taxpayer and liberally in favor of the taxing authority, and the

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[27] *Commissioner of Internal Revenue vs. Philippine National Bank*, G.R. No. 161997, October 25, 2005, citing Black's Law Dictionary, 8th Ed., pp. 1496-1497.
[28] *Commissioner of Internal Revenue vs. Pilipinas Shell Petroleum Corporation*, G.R. No. 188497, April 25, 2012.

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taxpayer bears the burden of establishing the factual basis of his claim for a refund.[29]

WHEREFORE, in light of the foregoing considerations, the instant *Petition for Review* is **GRANTED.** The Decision dated October 19, 2017 and the Resolution dated February 1, 2018 rendered by the Third Division of this Court, in CTA Case No. 9088 are hereby **REVERSED and SET ASIDE**.

SO ORDERED.

ERLINDA P. UY
Associate Justice

WE CONCUR:

ROMAN G. DEL ROSARIO
Presiding Justice

JUANITO C. CASTAÑEDA, JR.
Associate Justice

ESPERANZA R. FABON-VICTORINO
Associate Justice

CIELITO N. MINDARO-GRULLA
Associate Justice

(With Concurring and Dissenting Opinion)
MA. BELEN M. RINGPIS-LIBAN
Associate Justice

(With Concurring and Dissenting Opinion)
CATHERINE T. MANAHAN
Associate Justice

JEAN MARIE A. BACORRO-VILLENA
Associate Justice

MARIA ROWENA MODESTO-SAN PEDRO
Associate Justice

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[29] *Philippine Long Distance Telephone Company vs. Commissioner of Internal Revenue*, G.R. No. 157264, January 31, 2008.

CERTIFICATION

Pursuant to Article VIII, Section 13 of the Constitution, 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.

ROMAN G. DEL ROSARIO
Presiding Justice

REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

EN BANC

COMMISSIONER OF INTERNAL REVENUE,
Petitioner,

-*versus*-

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

CTA *EB* NO. 1788
(CTA Case No. 9088)

Present:

Del Rosario, *P.J.*
Castaneda, Jr.,
Uy,
Fabon-Victorino,
Mindaro-Grulla,
Ringpis-Liban,
Manahan,
Bacorro-Villena, *and*
Modesto-San Pedro, *JJ.*

Promulgated:
OCT 03 2019
2:28 p.m.

x- -x

CONCURRING AND DISSENTING OPINION

MANAHAN, *J.*:

The *ponencia* granted the Petition for Review and reversed the Decision of the Third Division of this Court and consequently denied the claim for refund filed by respondents of alleged erroneously collected income tax on compensation income for taxable year 2012.

With all due respect to the majority of my esteemed colleagues, I disagree with the said ruling denying the claim for refund of respondents for taxable year 2012.

The overall conclusion granting the Petition for Review filed by petitioner Commissioner of Internal Revenue (CIR) is anchored on the premise that the salaries and emoluments of the Filipino officers and employees of the Asian Development Bank (ADB) are subject to income tax notwithstanding the provisions of the ADB Charter exempting officers and staff of the ADB from taxation.

I firmly adhere to the majority's reasoning that the taxation of income received by respondents, being resident Filipino employees of the ADB, is anchored on the pertinent provisions of the 1997 National Internal Revenue Code (NIRC) and as such is not exempt. My position is that the relevant law and the treaties so far proved that such exemption provided in the said ADB Charter is not clear and categorical and I have consistently adopted this in several promulgated decisions assigned to me as ponente.[1]

I do, however, express my opposition to the denial of the claims for refund of the respondents with regard to the income taxes they paid for taxable year 2012.

The provisions of Revenue Memorandum Circular (RMC) No. 31-2013 issued on April 12 2013, should be applied prospectively in light of the conflicting positions taken by the representatives of the Bureau of Internal Revenue (BIR) prior to the issuance of said RMC. The pronouncements made by officials of the BIR as to the taxability of the compensation received by the Filipino employees of ADB leaned more towards exemption from income taxes, causing the latter to believe that no taxes on their compensation income should be paid.

Allow me to quote portions of the decision promulgated by the Court in Division (with the undersigned as ponente) in the case entitled *Rowena Vicente, et.al., vs. Commissioner of Internal Revenue,* where I held the position that the principles of fair play and substantial justice dictate that the provisions of RMC No. 31-2013 should apply only prospectively, and I quote:

> "In saying this, it is vital at this point to legally scrutinize the application of the provisions of RMC 31-2013 to the instant claims for refund.

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[1] Cristeta May Galang, et.al., vs. CIR, CTA Case No. 9081, June 8, 2017; Rowena Vicente, et.al., vs. CIR, CTA Case No. 9096, July 7, 2017.

Section 7 of RMC 31-2013 clearly provides that the provisions thereof "shall take effect immediately" which means that it should take effect starting May 2, 2013 the date when a copy thereof was officially submitted to the Office of the National Administrative Register of the UP Law Center pursuant to the requirement of the Administrative Code, Section 3, Chapter 2, Book VII, which provides:

> Filing : (1) Every agency shall file with the University of the Philippines Law Center three (3) certified copies of every rule adopted by it. Rules in force on the date of effectivity of this Code which are not filed within three (3) months from the date shall not thereafter be the basis of any sanction against any party or persons.

Pursuant to the abovementioned provision, the Supreme Court emphasized in *National Association of Electricity Consumers for Reforms v. Energy Regulatory Commission, G.R. No. 163935, February 2, 2006* that both the requirements of publication and filing of administrative issuances are mandatory for their effectivity."

However, despite these clear wordings on its effectivity, respondent still proceeded to collect income tax payments from petitioner starting 2012. Seen against the backdrop of confirmations and affirmations of various revenue officials that their income was subject to lower income tax rates or to zero income tax until the issuance/publication of RMC No. 31-2013, the principles of fair play and substantial justice dictate that its provisions should apply to claims starting only from 2013 and onwards."

For reasons aforestated, I vote to **DENY** the Petition for Review filed by the CIR and grant the claims for refund covering the income taxes paid by respondents on their compensation income earned in 2012.

CATHERINE T. MANAHAN
Associate Justice

REPUBLIC OF THE PHILIPPINES
COURT OF TAX APPEALS
QUEZON CITY

EN BANC

COMMISSIONER OF INTERNAL REVENUE, *Petitioner,*	**CTA EB NO. 1788** **(CTA Case No. 9088)**
-versus-	
	Present: **Del Rosario,** *P.J.,* **Castañeda, Jr.,** **Uy,** **Fabon-Victorino,** **Mindaro-Grulla,** **Ringpis-Liban,** **Manahan,** **Bacorro-Villena,** *and* **Modesto-San Pedro,** *JJ*
SPOUSES MICHAEL GAVIN RICHARD L. DE LOS REYES AND JENNIFER C. CO-DE LOS REYES, *Respondents.*	**Promulgated:** **OCT 03 2019** 2:28 p.m.

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CONCURRING AND DISSENTING OPINION

RINGPIS-LIBAN, J.:

With all due respect to the ponencia of my esteemed colleague, Hon. Erlinda P. Uy, which granted the Petition for Review that reversed and set aside the Decision of the Third Division of this Court which ordered the refund in favor of Spouses Michael Gavin Richard L. De Los Reyes and Jennifer C. Co- De Los Reyes, the amount of One Million Nine Hundred Forty-Eight Thousand Eight Hundred Thirty-Two and 34/100 Pesos (P1,948,832.34), representing their erroneously collected income tax on compensation from Asian Development Bank (ADB) for calendar year 2012, I concur with the finding that the relevant treaty and legislative provisions demonstrate that Congress really intended to tax the salaries and emoluments received by the Filipinos from ADB and that the Regional Trial Court Decision in Civil Case No. MC14-8775 (RTC Decision) declaring void Section 2 (d) (1) of Revenue Memorandum Circular 31-2013 does not constitute a binding precedent.

However, as regards the propriety of enforcing RMC 31-2013 to respondents' income from the ADB for calendar year 2012, while I agree with the ponencia that RMC 31-2013 is an interpretative rule, I believe that Justice and Equity dictate that it should be applied prospectively.

RMC 31-2013 was issued by petitioner in calendar year 2013. Nonetheless, petitioner subjected respondents' income for the previous year (i.e., calendar year 2012) to income tax. In the past, however, compensation income of resident citizens employed by foreign governments and/or international organizations were not subjected to income tax.

Section 7 of RMC 31-2013 clearly provides that the provisions thereof "shall take effect immediately" which means that it should take effect starting May 2, 2013 the date when a copy was officially submitted to the Office of the National Administrative Register of the UP Law Center pursuant to the requirement of the Administrative Code, Section 3, Chapter 2, Book VII, which provides:

> "Filing. (1) Every agency shall file with the University of the Philippines Law Center three (3) certified copies of every rule adopted by it. Rules in force on the date of effectivity of this Code which are not filed within three (3) months from the date shall not thereafter be the basis of any sanction against any party or persons."

In National Association of Electricity Consumers for Reforms v. Energy Regulatory Commission[1], the Supreme Court reiterated that both the requirements of publication and filing of administrative issuances are mandatory for their effectivity. The National Association case was promulgated in 2006 and the doctrine regarding the effectivity of administrative issuances has not been overturned to this day. Even if the date of filing of RMC 31-2013 is used as the reckoning point of its effectivity, specifically, May 2, 2013, the taxable period in which respondent wishes to impose the subject administrative issuance on petitioner, TY 2012, is one in which the said RMC was still non-existent. The only way it can be made to apply to that specific taxable period is if RMC 31-2013 were to be applied retroactively which, if done, would be anathema to the principles of justice and fair play.

For one thing, it is to be noted that prior to RMC 31-2013, in addition to the long standing practice of not taxing the income tax of Filipino ADB

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[1] G.R. No. 163935, February 2, 2006.

personnel, revenue officials have made various pronouncements regarding the subject when queried.

First, in BIR Ruling No. 029-99 dated March 11, 1999, the former BIR Commissioner, Beethoven Rualo, stated as follows:

> "Such being the case, Filipinos employed and are occupying managerial and technical positions as those of aliens employed by the bank x x x are subject to the preferential tax of 15% of their gross compensation income."

Second, in a Letter Opinion dated January 29, 2001[2], BIR Regional Director Antonio Ortega confirmed that officers and staff of the ADB need not secure Tax Identification Numbers (TINs) since their salaries are exempt from taxation.

Third, in an opinion issued by the Chief of the Legal Division of Revenue Region No. 7 dated February 6, 2013, Amado Rey B. Pagarigan reiterated the opinion of Mr. Rualo and stated that the Filipino employees of ADB are subject to the preferential tax rate of 15% on their compensation income.

From being taxed at a preferential tax rate of 15% on their compensation income to being exempted from being taxed at all, at any rate, the opinions given by revenue officials on the matter have been inconsistent, to say the least. Both the ADB and its Filipino resident employees who have relied on these inconsistent rulings by the BIR should not be faulted for relying thereon.

It was only when RMC 31-2013 was issued that then Commissioner Kim Henares categorically clarified that they are subject to tax. Pertinent portions of the said RMC are quoted below:

> "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:
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> xxx xxx xxx
>
> From the above, only officers and staff of the ADB who are not Philippine nationals shall be exempt from Philippine income tax." (Emphasis supplied)

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[2] Id. at Note 4, pp. 34-35.

Considering the foregoing, the fundamental principles of fairness and equity dictate that the non-retroactive rule under Section 246 of the Tax Code be applied in this case. Section 246 provides, as follows:

> "SEC. 246. Non-Retroactivity of Rulings. — Any revocation, modification or reversal of any of the rules and regulations promulgated in accordance with the preceding Sections or any of the rulings or circulars promulgated by the Commissioner shall not be given retroactive application if the revocation, modification or reversal will be prejudicial to the taxpayers, except in the following cases:
> (a) Where the taxpayer deliberately misstates or omits material facts from his return or any document required of him by the Bureau of Internal Revenue;
> (b) Where the facts subsequently gathered by the Bureau of Internal Revenue are materially different from the facts on which the ruling is based; or
> (c) Where the taxpayer acted in bad faith." (Emphasis supplied)

In the case of ABS-CBN Broadcasting Corporation vs. Court of Tax Appeals[3], the Supreme Court rejected the retroactive application of rulings and circulars when such would cause prejudice to the taxpayers, thus:

> "It is clear from the foregoing that rulings or circulars promulgated by the Commissioner of Internal Revenue have no retroactive application where to so apply them would be prejudicial to taxpayers. The prejudice to petitioner of the retroactive application of Memorandum Circular No. 4-71 is beyond question. It was issued only in 1971, or three years after 1968, the last year that petitioner had withheld taxes under General Circular No. V-334. The assessment and demand on petitioner to pay deficiency withholding income tax was also made three years after 1968 for a period of time commencing in 1965. Petitioner was no longer in a position to withhold taxes due from foreign corporations because it had already remitted all film rentals and no longer had any control over them when the new Circular was issued. And in so far as the enumerated regulations promulgated by the Commission
>
> xxx xxx xxx
>
> Without doubt, private respondent would be prejudiced by the retroactive application as it would be assessed of deficiency excise tax." (Emphasis supplied)

[3] G.R. No. L-52306 dated October 12, 1981.

The non-retroactivity principle was later on reiterated in Commissioner of Internal Revenue vs. Court of Appeals, Court of Tax Appeals and Alhambra Industries, Inc.,[4] where the Supreme Court emphasized the following:

> "However, well entrenched is the rule that rulings and circulars, rules and regulations promulgated by the CIR would have no retroactive application if to so apply them would be prejudicial to the taxpayers.
>
> xxx xxx xxx
>
> "Without doubt, private respondent would be prejudiced by the retroactive application as it would be assessed of deficiency excise tax."

It is readily apparent that the retroactive application of the provisions of RMC 31-2013 to income received by the respondents in 2012 made prior to its publication in 2013 already caused serious prejudice to the Filipino employees of the ADB. Due to lack of notice on the taxability of their income for TY 2012, none of the ADB Filipino employees were prepared to incur such huge tax obligations. They were not given a chance to allot or budget their finances to account for this debt to the government that they were blindsided with. Neither were they prepared to face the consequences of being unable to pay the same such as the prospect of law suits and potential garnishment of their bank deposits.

In this case, respondents received the compensation income being subject to income tax in calendar year 2012. During this period, respondents believed in good faith that their compensation income was exempt from tax. Prior to the issuance of RMC 31-2013, petitioner did not enforce any rules that would lead respondents to believe otherwise. When petitioner issued RMC 31-2013 and sought to enforce its provisions subjecting compensation income of resident citizens employed by ADB to the graduated income tax rates immediately, respondents were constrained to file their Income Tax Return for calendar year 2012 and pay the amount of P1,948,832.34. Whereas previously, respondents' income was not subjected to tax, they now had to come up a substantial amount in order to settle their income tax liability.

Considering that none of the exceptions in Non-Retroactivity Rule exist to bar its application in the instant case, I believe that RMC No. 31-2013 should be applied prospectively in the interest of justice and equity.

In view of the foregoing, I vote to DENY the Petition for Review, and AFFIRM the assailed Decision dated October 19, 2017 and the assailed Resolution dated February 1, 2018, and ORDER petitioner Commissioner of

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[4] G.R. No. 117982 dated February 6, 1997.

Internal Revenue to refund in favor of respondents Spouses Michael Gavin Richard L. De Los Reyes and Jennifer C. Co- De Los Reyes, the amount of One Million Nine Hundred Forty-Eight Thousand Eight Hundred Thirty-Two and 34/100 Pesos (P1,948,832.34, representing their erroneously collected income tax on compensation from Asian Development Bank for calendar year 2012.

MA. BELEN M. RINGPIS-LIBAN
Associate Justice