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

Section 34 (F) (3) of the Tax Code of 1997, as amended
BIR Ruling No. 728-2019; BIR Ruling No. 598-2012
OT- 353-2022
JUL 19 2022

COCA-COLA FEMSA PHILIPPINES, INC.
27F Net Lima Building, 5th Avenue corner 26th Street
Bonifacio Global City, Taguig City

Attention: ATTY. NIGEL AVILA
Tax Manager

Gentlemen:

This refers to your request on behalf of **Coca-Cola FEMSA Philippines, Inc.**[1] **("CCFPI" for brevity)**, for confirmation on the proposed change in accounting treatment for bottles and cases in claiming depreciation, both for tax and financial accounting purposes.

Background:

CCFPI is a domestic corporation engaged in the manufacture, distribution and sale of non-alcoholic beverages, including juices and water.

As of December 31, 2016, CCFPI is 51% owned by Controladora de Inversiones de Bebidas, S.L. while Coca-Cola South Asia Holdings, Inc. and Coca-Cola Holdings (Overseas) Ltd. owns 39% and 10% respectively. Controladora de Inversiones de Bebidas, S.L. is a wholly owned subsidiary of Coca-Cola FEMSA, S.A.B. de C.V.

CCFPI currently treats its bottles and cases based on the old policy of its previous owner. Approximately thirty percent (30%) is recorded as inventory and seventy percent (70%) is recorded as property, plant, and equipment, as follows:

Classification	Balance Sheet Treatment	
	Inventory (Approximately)	Fixed Assets (Approximately)
Bottles	30%	70%
Cases	30%	70%

With the change in ownership, CCFPI needs to align the accounting treatment of its assets in accordance with the accounting treatment per Coca-Cola FEMSA, S.A.B. de C.V. policy, as follows:

Classification	Balance Sheet Treatment	
	Inventory	Fixed Assets
Bottles	0%	100%
Cases	0%	100%

[1] Formerly: Coca-Cola Bottlers Philippines, Inc.
Now: Coca-Cola Beverages Philippines, Inc.

From the foregoing, CCFPI proposes to change the accounting treatment of bottles and cases starting January 1, 2017, as follows:

Classification	Balance Sheet Treatment		
	Inventory	Fixed Assets	Useful Life
Bottles	0%	100%	4 years
Cases	0%	100%	7 years

With the said changes, CCFPI will now be recognizing depreciation on the said assets. Based on the Affidavit dated April 05, 2021 of Mr. Erwinson C. Baltazar, the Controller of CCFPI, below is the financial comparison of the effect of the change in accounting treatment of the said assets, as follows:

Type of Asset	Depreciation using old accounting treatment (Php)	Depreciation using new accounting treatment (Php)	Difference (Php)
Bottles (2017)			
Bottles (2018 onwards)			
Cases (2017)			
Cases (2018 onwards)			

Per Letter dated March 08, 2022 of Mr. Romano Maglalang, the Senior Tax Manager of CCFPI, the latter is still collecting deposit value of the bottles for every sale of Coca-Cola products in Returnable Glass Bottles (RGB). The deposit value forms part of Accounts Receivable from customers and Container Deposit Liability accounts, subject for reversal once glass bottles are returned. For every unreturned bottle, the customer shall pay the corresponding deposit value to CCFPI. The amount covered by customers' deposit shall be deducted from the depreciation expense recorded in CCFPI's books amortized over the asset's useful life.

In reply thereto, please be informed that Section 34 (F) (1) of the National Internal Revenue Code (Tax Code) of 1997, as amended, provides that there shall be allowed as a depreciation deduction a reasonable allowance for the exhaustion, wear and tear (including reasonable allowance for obsolescence) of property used in the trade or business.

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

a. The straight-line method;

b. Declining-balance method, using a rate not exceeding twice the rate which would have been used had the annual allowance been computed under the method described in Subsection (F) (1);

c. The sum-of-the-years-digit method; and

d. Any other method which may be prescribed by the Secretary of Finance upon recommendation of the Commissioner. [Sec. 34 (F) (2), Tax Code of 1997, as amended]

Corollarily, Section 34 (F) (3) of the Tax Code of 1997, as amended, provides that —

"SEC. 34. Deductions from Gross Income. - Except for taxpayers earning compensation income arising from personal services rendered under an employer-employee relationship where no deductions shall be allowed under this Section, in computing taxable income subject to income tax under Sections

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24(A); 25(A); 26; 27(A), (B), and (C); and 28(A)(1), there shall be allowed the following deductions from gross income:

xxx xxx xxx

(F) Depreciation. –

xxx xxx xxx

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

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

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

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

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

"Section 109. Method of computing depreciation allowance. — The capital sum to be replaced should be charged off over the useful life of the property, either in equal instalment or in accordance with any other recognized trade practices, such as an apportionment of the capital sum over units of production. Whatever plan or method of apportionment is adopted must be reasonable and must have due regard to operating conditions during the taxable period. While the burden of proof must rest upon the taxpayer to sustain the deductions taken by him, such deductions must not be disallowed unless shown by clear and convincing evidence to be unreasonable. The reasonableness of any claim for depreciation shall be determined upon the conditions known to exist at the end of the period for which the return is made.

If it develops that the useful life of the property will be longer or shorter than useful life as originally estimated under all the then known facts, the portion of the cost of other basis of the property not already provided for through depreciation allowances should be spread over the remaining useful life of the property as re-estimated in the light of the subsequent facts, and depreciation deductions taken accordingly. " (Emphasis supplied)

Based on the foregoing, the taxpayer and the Commissioner may agree on the estimated useful life and rate of depreciation of any property. The rate so agreed upon shall be binding on both the taxpayer and the Bureau of Internal Revenue (BIR). However, if it develops that the useful life of the property originally estimated under previous factual conditions is no longer reasonable, the law allows the taxpayer to lengthen or shorten the useful life of the property in the light of prevailing factual considerations.[2]

In view of the foregoing, this Office hereby confirms the proposed change in accounting treatment of the above-mentioned assets of CCFPI in claiming depreciation, both for tax and financial accounting purposes, effective January 1, 2017 pursuant to the provisions of Section 34 (F) of the Tax Code of 1997, as amended, provided, however, that any prior period adjustments shall be subject to deficiency income tax, interest and penalties, if warranted.[3] Provided further, that amounts collected for unreturned bottles must be reported as income of CCFPI and must be deducted from depreciation expense claimed by CCFPI.

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

Very truly yours,

Lilia C. Guillermo

LILIA CATRIS GUILLERMO
Commissioner of Internal Revenue

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[2] BIR Ruling No. 598-2012 dated October 25, 2012
[3] BIR Ruling No. 728-2019 dated December 9, 2019