



	Individual	Professional Partnership	Corporation/Co-Partnership
Gross Sales or Gross Receipts			5,000,000
Less: Cost of Goods Sold			(3,000,000)
Gross Income			2,000,000
Less: Optional Standard Deduction	bojnr		
(5,000,000 x 40%)	(2,000,000)	(2,000,000)	

Changing the Tax Base for

OPTIONAL STANDARD DEDUCTION

A Move to Equalize Individual and Corporate Availment



by

**ELVIRA P. CRUDO**  
 Director II, Direct Taxes Branch

**Introduction**

Under Section 34(L) of the National Internal Revenue Code of 1997 (Tax Code), as amended, an **individual** subject to tax under Section 24, other than a nonresident alien, may elect a standard deduction in an amount not exceeding 40% of his gross sales or gross receipts, as the case may be. On the other hand, a **corporation** subject to tax under Sections 27(A) and 28(A)(1) thereof may elect a standard deduction in an amount not exceeding 40% of its gross income.

**Historical Changes in Determining the Optional Standard Deduction (OSD)**

Previous Tax Base

The 1993 edition of the Tax Code<sup>1</sup> states that OSD shall be equivalent to 10% of an individual’s gross income, while corporations are given 40% OSD based on gross income. Thus, while the OSD given to an individual taxpayer is **in lieu of** the itemized deductions or operating expenses, and the cost of goods sold, the OSD given to corporations is **on top of** the cost of sales or services.

<sup>1</sup> Nollo, Jose N. and Nollo, Mercedita, S. The National Internal Revenue Code of the Philippines, 1993, 16<sup>th</sup> and Revised Edition.

## Present Tax Base

Section 3 of the Bureau of Internal Revenue (BIR) Revenue Regulations (RR) No. 16-2008, the implementing regulations of RA No. 9504<sup>2</sup>, grants individual taxpayers an OSD equivalent to a maximum of 40% of gross sales or gross receipts during the taxable year. On the other hand, corporate taxpayers are allowed OSD to an amount not exceeding 40% of their gross income<sup>3</sup>.

Shown below is an illustrative computation for both individual and corporate taxpayers engaged in the same business, having the same revenue of P300,000.00, and cost of sales of P120,000.

Table A		Table B	
INDIVIDUAL TAXPAYER		CORPORATE TAXPAYER	
Gross Sales or Gross Receipts	P 300,000.00	Gross Sales	P 300,000.00
		Less: Cost of Goods Sold	120,000.00
		Gross Income	P 180,000.00
Less: 40% OSD	120,000.00	Less: 40% OSD	72,000.00
<b>Net Income subject to tax</b>	<b>P 180,000.00</b>	<b>Net Income subject to tax</b>	<b>P 108,000.00</b>

Due to the adoption of gross income as basis for the computation of OSD, a corporate taxpayer (as seen in Table B) generates a lower amount of taxable income (P108,000.00) compared to an individual taxpayer (Table A), who has taxable income of P180,000.00 using gross sales or gross receipts as his OSD base.

Evidently, this disparity in the computation of OSD makes the tax base for corporations more favorable than that of self-employed individuals. Though personal and additional exemptions are allowed for individual taxpayers, the effect of such exemptions will be minimal compared to the increases in the level of gross sales/ receipt.

### Revenue Loss When OSD Was Granted to Corporations

The fiscal impact of RA No. 9504<sup>4</sup> cannot be discounted. According to former BIR Commissioner Joel L. Tan-Torres, the amount of revenue losses reported in 2009 by the Bureau's Large Taxpayers Service, which collects 75.45% of total income tax collections from corporate taxpayers, were estimated at P5.003 Billion for that year<sup>5</sup>.

It clearly shows that OSD based on gross income results to lower income tax collection because deductible expenses such as cost of goods sold and other direct expenses generate lower taxable income.

### Other Studies Made and Positions Taken

The 2012 Review of the Optional Standard Deduction<sup>6</sup> showed the following findings:

- Based from the experience of private accounting firms engaged in tax and audit services, the determination of whether OSD or itemized deduction is to be used, is determined by the nature of taxpayer's business.
  - For businesses whose expenses/deductions are difficult to determine, the OSD is the more practical alternative,
  - For businesses that do not normally incur expenses beyond the 40% limit, the OSD would result to lower taxable income.
- As a general rule, in order to claim an expense as a deductible item, its direct relation to the business activity must be established. The record-keeping process for both methods entails effort and vigilance. Since an individual taxpayer using OSD is no longer required to submit records to substantiate gross sales or gross receipts, many taxpayers find the OSD as being administratively easier.
- The disparity of resulting taxable income for individual and corporate taxpayers as a consequence of RA 9504 leans against the individuals and favors corporations. In effect, it does not promote fairness among taxpayers.

<sup>2</sup> RA 9504 entitled "An Act Amending Section 22, 24, 34, 35, 51, and 79 of Republic Act No. 8424, As Amended, Otherwise Known as the National Internal Revenue of 1997," passed on June 17, 2008.

<sup>3</sup> Section 5 of RR No. 16-2008; Sections 27(A) and 28(A)(1) of the Tax Code.

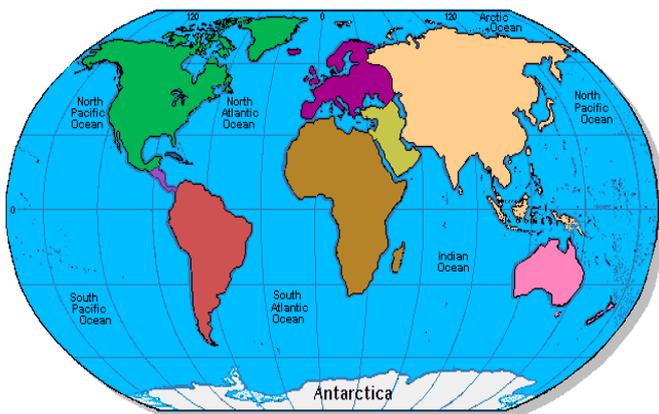
<sup>4</sup> Section 3 of RA 9504.

<sup>5</sup> BIR Letter to STSRO with Subject "Revenue Impact of Availment of Optional Standard Deduction (OSD)" dated January 18, 2009.

<sup>6</sup> STSRO Review of the Optional Standard Deduction, June 20, 2012.

4. According to the Department of Finance, OSD is really intended to help the unsophisticated taxpayer or small taxpayers who cannot hire tax accountants in filing an income tax return. It is not meant to be a tool to deliberately reduce the income tax due of a taxpayer. However, the Bureau of Internal Revenue noted an increasing number of corporations, especially the large ones, which uses OSD to reduce their income tax liabilities.

### Situation in Other Tax Jurisdictions



1. In American tax law, standard deduction is the portion of an individual's or couple's income that is not taxed which is computed after arriving at the adjusted gross income. It is an Internal Revenue Service (IRS) specified amount by which a taxpayer is entitled to reduce income. It is considered as an alternative to itemizing deductions<sup>7</sup>. In other words, taxpayers are given the option to choose between the standard deduction and itemized deductions.<sup>8</sup>
2. In Thailand<sup>9</sup>, a standard deduction is allowed in terms of percentage of assessable income or the actual expenses incurred in deriving income depending in the category of income. For a certain type of income, a standard deduction of 40% with a maximum deduction of Baht 60,000 (P80,040.00)<sup>10</sup> is allowed.

In the case of a lump-sum payment due to retirement or termination, the standard deduction is Baht 7,000 (P9,338.00)<sup>11</sup> multiplied by the number of years of employment, but not in excess of the payment itself. A further deduction of 50% is available for the balance.

Except for income from copyrights for which a standard deduction of 40%, with a maximum deduction of Baht 60,000 (P80,040.00) is allowed, no deduction of expenses is allowed for certain types of income.<sup>12</sup>

On the other hand, for income under Sections 40 (5) to 40(8) of Thailand Tax Code, either the actual expenses incurred in deriving such income or alternatively the optional standard deductions ranging from 10% to 85% in respect of each category of income is allowed.

3. In Taiwan<sup>13</sup>, taxpayers are entitled to deductions and personal exemptions. These are given as a choice between the optional standard deduction and itemized deductions. The standard deduction is TWD 76,000 (P110,108.80)<sup>14</sup> for single taxpayers and TWD 152,000 (P220,217.60)<sup>15</sup> for married taxpayers. Further, a taxpayer who elects the standard deduction option is still entitled for some special deductions, such as losses from property transactions, deductions for salary and wage earners, deductions for savings and investments, for the disabled and handicapped, and education fees of dependent children, among others.



<sup>7</sup> Campbell R. Harvey (2012). Retrieved March 18, 2015 from [www.financial-dictionary.the.free.dictionnary.com](http://www.financial-dictionary.the.free.dictionnary.com).

<sup>8</sup> Farley Financial Dictionary. 2012 Farlex, Inc. Retrieved June 8, 2015 [www.financial-dictionary.free.dictionnary.com](http://www.financial-dictionary.free.dictionnary.com).

<sup>9</sup> Tilleke & Gibbins International Ltd. A Summary of Thailand's Tax Laws, March 2009.

<sup>10</sup> BSP Reference Rate of Peso Equivalent to Thailand Baht 1.334 (60,000 x 1.334= P80,040.00)

<sup>11</sup> 7,000 x 1.334 = P9,338

<sup>12</sup> Sections 40(3) and (4) of Thailand Tax Code.

<sup>13</sup> Grant Thornton, An Instinct for Growth, 2014.

<sup>14</sup> BSP Reference Rate of Peso Equivalent to Taiwan NT Dollar 1.4488 (76,000 x 1.4488= P110,108.80)

<sup>15</sup> 152,000 x 1.4488 = P220,217.60

# TAX NEWS DIGEST

**“Gov’t to miss poverty-reduction target. 19% goal for 2016 falls short of global commitment”.**



Socio-economic Planning Secretary Arsenio M. Balisacan. INQUIRER FILE PHOTO

“The government has conceded that it would be unable to reduce poverty this year to the levels it had earlier committed under the United Nations’ Millennium Development Goals (MDGs) for 2015 aimed at improving human life in general.

“In a speech before members of the Foreign Correspondents Association of the Philippines, Economic Planning Secretary Arsenio M. Balisacan noted that while strides have been made by the Aquino administration to grow the economy, it was still working hard to address the remaining problems of poverty and unemployment.

population by next year, according to Balisacan, who is also director general of the National Economic and Development Authority (NEDA).

“But the Neda chief admitted that the 2016 poverty-reduction goal “will fall short of the Millennium Development Goals target of 16.6 by 2015, or half of the poverty incidence of about 33 percent in 1991.” (PDI, February 12, 2015)



**“PH banks report 8.17% decline in '14 profit. Stiff capital requirements blamed for industry performance”.**



Bangko Sentral ng Pilipinas. INQUIRER.net FILE PHOTO

“Profits of the country’s largest banks declined last year as the cost of money went up and stricter regulations that called for higher capital buffers took effect, data released by the central bank showed.

“In a report, the Bangko Sentral ng Pilipinas (BSP) said the country’s 36 universal and commercial banks saw interest margins slim. Although this was slightly offset by lower funding costs, total yields still fell, leading to an industry-wide decline in return on equity.

down year-on-year.

“Net interest income in 2014 rose to P261.75 billion, higher by 17 percent from P223.19 billion in 2013. However, non-interest income took a dive to P127.49 billion from P152.83 billion, while non-interest expense rose to P238.99 billion from P223.49 billion.

“The BSP said the banks’ net interest margin declined by two-tenths of a percent to 2.99 percent from 3.01 percent.” (PDI, February 12, 2015)



### **“DOF eyeing new revenue sources.”**



“Department of Finance (DOF) officials are set to propose new revenue sources as other government agencies are bent on slashing not only income but also corporate tax rates.

“In an interview last week, Finance Undersecretary Jeremias N. Paul Jr., said the DOF before the

end of February would submit to the Lower House a “package deal” of measures to make up for the revenue losses brought on by the income tax reform.

“Members of the House Committee on Ways and Means held a technical meeting to consolidate the pending bills that sought to reduce income tax rates.

“During the meeting, Paul maintained that the DOF would stick to its stance of putting in place a “comprehensive, non-piecemeal and, as much as possible, revenue-neutral” tax reform rather than just touching on the populist income taxation.” (PDI, February 16, 2015)

--- ❖ ---

### **“Cheaper oil brings down Customs take.”**



“Duties and taxes collected by the Bureau of Customs (BOC) slid year on year last January mainly due to cheaper oil, Commissioner John Phillip P. Sevilla last February 16, 2015.

“Without disclosing actual figures, Sevilla said last month’s collections were “lower” than the take in January last year.

“BOC data showed that it collected P29.772 billion during the first month of 2014, higher by 21.3 percent than the P24.540 billion collected in January 2013.

“The actual January 2014 collections, however, were lower by 4.9 percent than the goal for that

month of P31.307 billion.

“Sevilla said that in January this year, lower global oil prices pulled down collections, alongside the three-day holiday due to the visit of Pope Francis, during which port operations in Manila were shut down.” (PDI, February 17, 2015)

--- ❖ ---

### **“BIR collection up 9.64% in '14, missing goal. Total tax take 8.41% below the full-year target of P1.46T.”**



“Tax collections of the Bureau of Internal Revenue (BIR) in 2014 grew by almost a tenth, but fell short of the goal.

“The BIR collected P1.334 trillion in taxes last year, up 9.64 percent from P1.217 trillion in 2013, based on preliminary data presented by Commissioner Kim S. Jacinto-Henares at a forum hosted by the Center for Philippine Futuristics Studies and Management Incorporated.

“The 2014 take, however, was 8.41-percent below the target of P1.46 trillion.

“Henares later told reporters that since the figure she had presented was still “tentative” and unreconciled with the official figures to be released by the Bureau of the Treasury, the 2014 tax collection figure of the BIR could still go up.

“When asked why the BIR missed last year’s goal, Henares said “mataas ‘yong target (the target was high).”

“The preliminary data based on 1,209 reports of the BIR’s revenue district offices showed that the bulk or P1.297 trillion in collections last year was contributed by BIR operations.” (PDI, March 2, 2015)

❖ ---

## **“APEC aims for inclusive growth. Greater access to finance pushed”**



through greater access to finance and improved infrastructure under the proposed Cebu Action Plan.

“The Philippines, which hosts this year’s APEC meetings, has its own share of initiatives that target to make public-private partnership (PPP) in infrastructure more appealing to investors, such as expanding insurance coverage to projects being rolled out by local government units (LGUs), Philippine officials said on the sidelines of APEC Finance and Central Bank Deputies’ Meeting.

“Finance Undersecretary Gil S. Beltran noted that while the APEC jurisdiction is expected to post growth of 3.5 percent this year and a slightly higher 3.7 percent next year, there has been a “slowdown” in investments across the region.” (PDI, March 9, 2015)



## **“Foreign investments hit all-time high in '14. December inflows up more than 5x”**



“Long-term foreign investments in the Philippines rose last year to its highest level in history as the country reaped the benefits of its recent turnaround into one of the region’s growth leaders.

“The Bangko Sentral ng Pilipinas (BSP) said foreign direct investments (FDIs) rose more than fivefold in December alone, marking the 18th consecutive month that net inflows were recorded.

“FDI inflows remained robust, buoyed by strong investor confidence in the country’s solid macroeconomic fundamentals,” the BSP said in a statement on March 10, 2015.

“Last December, FDI net inflows rose to \$557 million from \$102 million in the same month the year before. For all of 2014, net inflows reached \$6.2 billion, up by two-thirds from 2013’s \$3.7 billion. Net inflows meant there were more investments than divestments by foreigners.

“Direct investments usually bankroll the construction of new facilities or the expansion of foreign firms’ new or existing operations in the country. These are considered a better barometer for the confidence of international investors in the country because these placements tie them to the economy’s fortunes for the long term.

“FDIs come in the form of equity placements in local companies and investments and loans by multinationals to their local affiliates and subsidiaries.

“Total investments for 2014 were higher than the average of \$2.2 billion in the four preceding years from 2010 to 2013.” (PDI, March 11, 2015)



## **“Asean regulators forge integrated banking pact. Deal will allow banks to operate in other parts of SE Asia”**



“Asian regulators have signed a definitive deal that will pave the way for the liberalization of the region’s banking industry, making money flow easier across borders.

“This comes as the region works for tighter integration, with the aim of tying each member countries’ economic prosperity to its neighbors.

“Bangko Sentral ng Pilipinas (BSP) Governor Amando M. Tetangco Jr. said the Association of Southeast Asian Nations (Asean) Banking Integration Framework (ABIF) was approved by central bank governors in Kuala Lumpur this March.

“The next step, he said, is for countries to start bilateral talks with neighbors to agree on more detailed terms over the operations of their banks.

“The framework allows Asean banks to operate in other member countries,” Tetangco told reporters this week.” (PDI, March 25, 2015)





- (1) **SILICON PHILIPPINES, INC., (formerly Intel Philippines Manufacturing, Inc.), Petitioner, vs. COMMISSIONER OF INTERNAL REVENUE (CIR), Respondent (G.R. No. 184360 and 184361, February 19, 2014).**
- (2) **CIR, Petitioner, vs. SILICON PHILIPPINES, INC., (formerly Intel Philippines Manufacturing, Inc.), Respondent (G.R. No. 184384, February 19, 2014).**

**Facts:**

*“For the 1<sup>st</sup> quarter of 1999, Silicon seasonably filed its Quarterly VAT Return on April 22, 1999 reflecting, among others, output VAT in the amount of P145,316.96; input VAT on domestic purchases in the amount of P20,041,888.41; input VAT on importation of goods in the amount of P44,560,949.00; and zero-rated export sales in the sum of P929,186,493.91.*

*“On August 6, 1999, Silicon filed with the CIR, through its One-Stop-Shop Inter-Agency Tax Credit and Duty Drawback Center of the Department of Finance (DOF), a claim for tax credit or refund of P64,457,520.45 representing VAT input taxes on its domestic purchases of goods and services and importation of goods and capital equipment which are attributable to zero-rated sales for the period January 1, 1999 to March 31, 1999.*

*“Due to the inaction of the CIR, Silicon filed a Petition for Review with the CTA on March 30, 2001, to toll the running of the two-year prescriptive period. The petition was docketed as CTA Case No. 6263.*

*“The CIR filed its Answer dated June 1, 2001 raising, among others, the following special and affirmative defenses: (1) that Silicon failed to show compliance with the substantiation requirements under the provisions of Section 16(c)(3) of Revenue Regulations No. 5-87, as amended by Revenue Regulations No. 3-88; and (2) that Silicon has not shown proof that the alleged domestic purchases of goods and services and importation of goods/capital equipment on which the VAT input taxes were paid are attributable to its export sales or have not yet been applied to the output tax for the period covered in its claim or any succeeding period and that the alleged total foreign exchange proceeds have been accounted for in accordance with the rules and regulations of the Bangko Sentral ng Pilipinas.”*

**Issue/s:**

*“The issues raised in the three petitions boil down to (1) whether the CTA En Banc correctly denied Silicon’s claim for refund or issuance of a tax credit certificate for its input VAT for its domestic purchases of goods and services and importation of goods/capital equipment attributable to zero-rated sales for the period January 1, 1999 to March 31, 1999; and (2) whether the CTA En Banc correctly ordered the CIR to refund or issue a tax credit certificate in favor of Silicon for the reduced amount of P2,139,431.00 representing Silicon’s unutilized input VAT attributable to its zero-rated sales for the period April 1, 2000 to June 30, 2000.”*

*“Notwithstanding the above issues, we emphasize that when a case is on appeal, this Court has the authority to review matters not specifically raised or assigned as error if their consideration is necessary in reaching a just conclusion of the case.*

*“In the present case, while the parties never raised as an issue the timeliness of Silicon’s judicial claims, we deem it proper to look into whether the petitions for review filed by Silicon before the CTA were filed within the prescribed period provided under the Tax Code in order to determine whether the CTA validly acquired jurisdiction over the petitions filed by Silicon.”*

**Held:**

*“After a careful perusal of the records in the instant case, we find that Silicon’s judicial claims were filed late and way beyond the prescriptive period. Silicon’s claims do not fall under the exception mentioned above. Silicon filed its Quarterly VAT Return for the 1<sup>st</sup> quarter of 1999 on April 22, 1999 and subsequently filed on August 6, 1999 a claim for tax credit or refund of its input VAT taxes for the same period. From August 6, 1999, the CIR had until December 4, 1999, the last day of the 120-day period, to decide Silicon’s claim for tax refund. But since the CIR did not act on Silicon’s claim on or before the said date, Silicon had until January 3, 2000, the last day of the 30-day period to file its judicial claim. However, Silicon failed to file an appeal within 30 days from the lapse of the 120-day period, and it only filed its petition for review with the CTA on March 30, 2001 which was **451 days late**. Thus, in consonance with our ruling in *Philex in the San Roque ponencia*, Silicon’s judicial claim for tax credit or refund should have been dismissed for having been filed late. The CTA did not acquire*

*jurisdiction over the petition for review filed by Silicon.*

*“Similarly, Silicon’s claim for tax refund for the second quarter of 2000 should have been dismissed for having been filed out of time. Records show that Silicon filed its claim for tax credit or refund on August 10, 2000. The CIR then had 120 days or until December 8, 2000 to grant or deny the claim. With the inaction of the CIR to decide on the claim which was deemed a denial of the claim for tax credit or refund, Silicon had until January 7, 2001 or 30 days from December 8, 2000 to file its petition for review with the CTA. However, Silicon again failed to comply with the 120+30 day period provided under Section 112(C) since it filed its judicial claim only on June 28, 2002 or **536 days late**. Thus, the petition for review, which was belatedly filed, should have been dismissed by the CTA which acquired no jurisdiction to act on the petition.*

*“Courts are bound by prior decisions. Thus, once a case has been decided one way, courts have no choice but to resolve subsequent cases involving the same issue in the same manner.*

*“As this Court has repeatedly emphasized, a tax credit or refund, like tax exemption, is strictly construed against the taxpayer. The taxpayer claiming the tax credit or refund has the burden of proving that he is entitled to the refund by showing that he has strictly complied with the conditions for the grant of the tax refund or credit. Strict compliance with the mandatory and jurisdictional conditions prescribed by law to claim such tax refund or credit is essential and necessary for such claim to prosper. Noncompliance with the mandatory periods, nonobservance of the prescriptive periods, and non adherence to exhaustion of administrative remedies bar a taxpayer’s claim for tax refund or credit, whether or not the CIR questions the numerical correctness of the claim of the taxpayer. For failure of Silicon to comply with the provisions of Section 112(C) of the NIRC, its judicial claims for tax refund or credit should have been dismissed by the CTA for lack of jurisdiction.”*

*Hence, for being filed out of time, Silicon’s judicial claims for refund were dismissed.*

**(3) COMMISSIONER OF INTERNAL REVENUE (CIR), Petitioner, vs. PILIPINAS SHELL PETROLEUM CORPORATION, Respondent (G.R. No. 188497, February 19, 2014).**

**Facts:**

Respondent in this case sold aviation fuel to international carriers and paid the excise tax thereon. Shell now seeks a refund of the same relying on Section 135 of the Tax Code.

Quoting the decision:

1. *“Respondent argues that a plain reading of Section 135 of the NIRC reveals that it is the petroleum products sold to international carriers which are exempt from excise tax for which reason no excise taxes are deemed to have been due in the first place.*
2. *“Respondent also contends that our ruling that Section 135 only prohibits local petroleum manufacturers like respondent from shifting the burden of excise tax to international carriers has adverse economic impact as it severely curtails the domestic oil industry.*
3. *“Lastly, respondent asserts that the imposition by the Philippine Government of excise tax on petroleum products sold to international carriers is in violation of the Chicago Convention on International Aviation (“Chicago Convention”) to which it is a signatory, as well as other international agreements (the Republic of the Philippines’ air transport agreements with the United States of America, Netherlands, Belgium and Japan).”*

**Issue/s:**

Are the above arguments tenable?

**Held:**

In deciding in favor of respondent, the Court emphasized:

*“Indeed, the avowed purpose of a tax exemption is always “some public benefit or interest, which the law-making body considers sufficient to offset the monetary loss entailed in the grant of the exemption.”<sup>15</sup> The exemption from excise tax of aviation fuel purchased by international carriers for consumption outside the Philippines fulfills a treaty obligation pursuant to which our Government supports the*

*promotion and expansion of international travel through avoidance of multiple taxation and ensuring the viability and safety of international air travel. In recent years, developing economies such as ours focused more serious attention to significant gains for business and tourism sectors as well. Even without such recent incidental benefit, States had long accepted the need for international cooperation in maintaining a capital intensive, labor intensive and fuel intensive airline industry, and recognized the major role of international air transport in the development of international trade and travel.*

*“Under the basic international law principle of pacta sunt servanda, we have the duty to fulfill our treaty obligations in good faith. This entails harmonization of national legislation with treaty provisions. In this case, Sec. 135(a) of the NIRC embodies our compliance with our undertakings under the Chicago Convention and various bilateral air service agreements not to impose excise tax on aviation fuel purchased by international carriers from domestic manufacturers or suppliers. In our Decision in this case, we interpreted Section 135 (a) as prohibiting domestic manufacturer or producer to pass on to international carriers the excise tax it had paid on petroleum products upon their removal from the place of production, pursuant to Article 148 and pertinent BIR regulations. Ruling on respondent’s claim for tax refund of such paid excise taxes on petroleum products sold to tax-exempt international carriers, we found no basis in the Tax Code and jurisprudence to grant the refund of an “erroneously or illegally paid” tax.*

“x x x.

*“We maintain that Section 135 (a), in fulfillment of international agreement and practice to exempt aviation fuel from excise tax and other impositions, prohibits the passing of the excise tax to international carriers who buys petroleum products from local manufacturers/sellers such as respondent. However, we agree that there is a need to reexamine the effect of denying the domestic manufacturers/sellers’ claim for refund of the excise taxes they already paid on petroleum products sold to international carriers, and its serious implications on our Government’s commitment to the goals and objectives of the Chicago Convention.*

*“The Chicago Convention, which established the legal framework for International civil aviation, did not deal comprehensively with tax matters. Article 24 (a)*

of the Convention simply provides that fuel and lubricating oils on board an aircraft of a Contracting State, on arrival in the territory of another Contracting State and retained on board on leaving the territory of that State, shall be exempt from customs duty, inspection fees or similar national or local duties and charges. Subsequently, the exemption of airlines from national taxes and customs duties on spare parts and fuel has become a standard element of bilateral air service agreements (ASAs) between individual countries.

“The importance of exemption from aviation fuel tax was underscored in the following observation made by a British author in a paper assessing the debate on using tax to control aviation emissions and the obstacles to introducing excise duty on aviation fuel, thus:

“Without any international agreement on taxing fuel, it is highly likely that moves to impose duty on international flights, either at a domestic or European level, would encourage ‘tankering’: carriers filling their aircraft as full as possible whenever they landed outside the EU to avoid paying tax. Clearly this would be entirely counterproductive. Aircraft would be travelling further than necessary to fill up in low-tax jurisdictions; in addition they would be burning up more fuel when carrying the extra weight of a full fuel tank.

“With the prospect of declining sales of aviation jet fuel sales to international carriers on account of major domestic oil companies’ unwillingness to shoulder the burden of excise tax, or of petroleum products being sold to said carriers by local manufacturers or sellers at still high prices, the practice of “tankering” would not be discouraged. This scenario does not augur well for the Philippines’ growing economy and the booming tourism industry. Worse, our Government would be risking retaliatory action under several bilateral agreements with various countries. Evidently, construction of the tax exemption provision in question should give primary consideration to its broad implications on our commitment under international agreements.

“In view of the foregoing reasons, we find merit in respondent’s motion for reconsideration. We therefore hold that respondent, as the statutory taxpayer who is directly liable to pay the excise tax on its petroleum products, is entitled to a refund or credit of the excise taxes it paid for petroleum products sold to international carriers, the latter having been granted exemption from the payment of said excise tax under Sec. 135 (a) of the NIRC.”



**TAXBITS is an official publication of the Senate Tax Study and Research Office (STSR) located at Rm. 524, Senate of the Philippines, Financial Center, Pasay City.**

Website : <http://www.senate.gov.ph>  
 Email : [stsr1989@gmail.com](mailto:stsr1989@gmail.com)  
 Facebook : <https://www.facebook.com/stsr.stsr>  
 Telefax No. : 552-6850; Local 5506, 5508

### Editors and Contributing Writers

**Atty. RODELIO T. DASCIL, MNSA**  
 Director General

**Atty. EMMANUEL M. ALONZO**  
 Director III, Legal & Tariff

**RECHILDA B. GASCON, MNSA**  
 Director III, Tax Policy & Admin

**MARIA LUCRECIA R. MIR, PhD DA, MNSA**  
 Director III, Direct Taxes

**VIVIAN A. CABILING**  
 Director III, Indirect Taxes

**JULIETA M. FONTIVEROS**  
 Director II, Legal & Tariff

**NORBERTO M. VILLANUEVA**  
 Director II, Tax Policy & Admin

**ELVIRA P. CRUDO**  
 Director II, Direct Taxes

**Atty. SHERRY ANNE C. SALAZAR**  
 Director II, Indirect Taxes

**BONIFACIO R. JOSON**  
 LSA-III, ODG - Layout Artist

**CLINTON S. MARTINEZ**  
 SLSO II, Indirect Taxes

The Articles were principally prepared by the authors, under the supervision of STSR Directors and the overall guidance of its Director-General. The views and opinions expressed are those of STSR and do not necessarily reflect those of the Senate, its leadership, or its individual members. For comments and suggestions, please email us at [stsr1989@gmail.com](mailto:stsr1989@gmail.com).