NATIONAL ADMINISTRATIVE REGISTER · OCTOBER 13, 2003

CLARIFYING THE TAX BASE FOR PURPOSES OF THE PERCENTAGE (GROSS RECEIPTS) TAX IMPOSED UNDER SECTIONS 121 AND 122 OF THE TAX CODE

BIR REVENUE MEMORANDUM CIRCULAR NO. 69-2003, October 13, 2003

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For information and guidance of all concerned, quoted hereunder are pertinent portions of the Supreme Court decision on the consolidated petitions for review of China Banking Corporation, petitioner vs. Court of Appeals, Court of Tax Appeals and Commissioner of Internal Revenue, respondents, G.R. No. 146749 and Commissioner of Internal Revenue, petitioner vs. China Banking Corporation, respondent G.R. No. 147938 dated June 10, 2003, which reiterated the position of the Bureau under Revenue Memorandum Circular No. 51-2002 dated November 14, 2002 that for purposes of the gross receipts tax, the basis of the tax should be the gross amount inclusive of the final withholding tax used in extinguishing the income tax liability of the recipient of the income, to wit:

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> "By its nature, a gross receipts tax applies to the entire receipts without deduction, exemption or exclusion, unless the law clearly provides otherwise."
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> "xxx xxx xxx"
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> "Moreover, when Section 121 of the Tax Code includes "interest" as part of gross receipts, it refers to the entire interest earned and owned by the bank without any deduction. "Interest" means the gross amount paid by the borrower to the lender as consideration for the use of the lender's money. Section 2(h) of Revenue Regulations No. 12-80, now Section 2(I) of Revenue Regulations No. 17-84, defines the term "interest" as "the amount which a depository bank (borrower) may pay on savings and time deposit in accordance with rates authorized by the Central Bank of the Philippines." This definition does not allow any deduction. The entire interest paid by the depository, without any deduction, is what forms part of the lending bank's gross receipts. To illustrate, assume that the gross amount of the interest income is P100. The lending bank owns this entire P100 since this is the amount the depository bank pays the lending bank for use of the lender's money. In its books the depository bank records an interest expense of P100 and claims a deduction for interest expense of P100. The 20% final withholding tax on this interest income is P20, which the law requires the depository bank to withhold and remit directly to the government. The depository bank withholds the final tax in trust for the government which then becomes the owner of the P20. The final tax is the legal liability of the lending bank as recipient of the interest income. The payment of the P20 final tax extinguishes the tax liability of the lending bank. The interest income that the depository bank turns over physically to the lending bank is P80, the net receipt after deducting the P20 final tax. Still, the interest income that forms part of the lending bank's gross receipts for purposes of the gross receipts tax is P100 because the total amount earned by the lending bank from its passive investment is P100, not P80. Stated differently, the lending bank paid P20 as final tax which is 20% of the interest income it received. Logically, the lending bank's interest income is P100 to arrive at a P20 final withholding tax. Since what the law includes in gross receipts is the interest income, then it is P100 and not P80 which forms part of the lending bank's gross receipts. If the lending bank's interest income is only P80, then its 20% final withholding tax should only be P16."
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> "xxx xxx xxx"

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> "Actual receipt of interest income is not limited to physical receipt. Actual receipt may either be physical receipt or constructive receipt. When the depository bank withholds the final tax to pay the tax liability of the lending bank, there is prior to the withholding a constructive receipt by the lending bank of the amount withheld. From the amount constructively received by the lending bank, the depository bank deducts the final withholding tax and remit it to the government for the account of the lending bank. Thus, the interest income actually received by the lending bank, both physically and constructively, is net interest plus the amount withheld as final tax. The concept of a withholding tax on income obviously and necessarily implies that the amount of the tax withheld comes from the income earned by the taxpayer. Since the amount of the tax withheld constitutes income earned by the taxpayer, then that amount manifestly forms part of the taxpayer's gross receipts. Because the amount withheld belongs to the taxpayer, he can transfer its ownership to the government in payment of his tax liability. The amount withheld indubitably comes from income of the taxpayer, and thus forms part of his gross receipt."
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> "xxx xxx xxx"
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> "The gross receipts tax falls not on the final withholding tax, but on the amount of the interest income withheld as the final tax. What is being taxed is still the interest income. The law imposes the gross receipts tax on the portion of the interest income that the depository bank withholds and remits to the government. Consequently, the entire amount of the interest income is taxable and not only the net interest income. Moreover, whenever the legislature excludes a certain tax from gross receipts, the legislature states so clearly and unequivocally.
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> "xxx xxx xxx"
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> "In summary, CBC has failed to point to any specific provisions of law allowing the deduction, exemption or exclusion from its taxable gross receipts, of the amount withheld as final tax. Such amount should therefore form part of CBC's gross receipts in computing the gross receipts tax."
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> "WHEREFORE, the Petition for Review filed by China Banking Corporation in G.R. No. 146749 is DENIED for lack of merit. The Petition for Review filed by the Commissioner of Internal Revenue in G.R. No. 147938 is GRANTED. The assailed decisions and resolutions of the Court of Tax Appeals in CTA Case No. 5405 and those of the Court of Appeals in CA G.R. SP No. 50839 and CA-G.R. SP No. 50790 are SET ASIDE. SO ORDERED."

All internal revenue officers and employees are hereby enjoined to give this Circular as wide a publicity as possible.

Adopted: 13 Oct. 2003

(SGD.) GUILLERMO L. PARAYNO, JR.
Commissioner of Internal Revenue

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