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Tax Controversy

Philippines

Du-Baladad and Associates Law Offices (BDB Law)

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Law and Practice

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Du-Baladad and Associates Law Offices (BDB Law) is a boutique law firm specialising in taxation and related corporate services. It offers a complete array of tax services, including high-end tax advisory, tax dispute resolution, tax litigation, mergers and acquisition, advocacy, tax compliance, transfer pricing and expatriate services, among others, and has defended hundreds of cases with the tax authority, resulting in the cancellation of hundreds of billions

of tax assessments. The team has 22 to 25 experienced tax professionals, mostly accountant-lawyers, who can appreciate the intricacies of transactions, thereby enabling them to provide sound and practical solutions from the standpoint of business and regulatory compliance. BDB Law is a member of WTS Global, a European TIER 1 global tax network represented in more than 100 countries.

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1. Tax Controversies

1.1 Tax Controversies in this Jurisdiction

For both national and local taxes, tax controversies in the Philippines primarily arise from the following:

- Tax self-assessment can trigger tax audit when a taxpayer declares a tax due in his or her tax return but does not pay the corresponding amount due as declared by him or her. A notice of tax delinquency is issued by the tax bureau, the Bureau of Internal Revenue (“BIR”).
- Regular tax investigations conducted by the tax authorities – the BIR for national taxes, the Bureau of Customs (“BOC”) for tariff and customs duties, and the Local Governments for local taxes. Local taxes are those imposed by provinces, cities and municipalities on income or properties within their respective jurisdictions.
- Claims for refunds by taxpayers for erroneously paid taxes, excess input VAT or excess withholding tax, which trigger a tax audit to determine if the claim is valid.
- Administrative decisions denying a taxpayer’s request for confirmatory rulings on the taxability of certain transactions may trigger an audit.
- Court decisions confirming the taxability of a transaction may also cause an audit on similar transactions, either singly or as an industry audit.

Tax Self-assessment

A self-assessed tax falls due without need of any prior examination by the BIR, and non-payment of a self-assessed tax on the date prescribed by law results in penalties even in the absence of any assessment by the BIR. While the taxpayer’s failure to pay a self-assessed tax when due may result in a subsequent investigation and assessment by the BIR, it does not remove the character of the tax as a self-assessed tax. The subsequent BIR investigation and assessment is for the purpose of collecting a past due tax, and not for the purpose of creating the tax liability. Of course, the computation by the taxpayer of his or her tax liability under a self-assessed tax is not conclusive on the BIR. After investigation or audit, the BIR can issue an assessment for any deficiency tax still due from the taxpayer.

Tax Investigations by Tax Authorities

The tax authority may conduct a tax investigation within three years of the last day prescribed by law for the filing of the return, or the actual date of filing, whichever is later. Based on the investigation conducted, if the examiner finds the taxpayer to have incorrectly paid its taxes, an official tax assessment shall be issued by the tax authority. The taxpayer may contest the assessments, at first administratively, and thereafter to the courts if the controversy is not settled at the administrative level.

Refund of Erroneously Paid Taxes or Excess Taxes Withheld

The taxpayer may claim a refund of erroneously paid internal revenue taxes or excess tax withheld within two years from the payment of the tax. The law requires that the administrative claim for refund must be made within two years from the payment of the tax. Similarly, the judicial claim must also be filed within two years from the date of payment of the tax. More often than not, the claims for refund filed with the tax authority are not acted upon right away, and instead subject the claimant to an audit, forcing the taxpayer to elevate the claim to the courts when the two-year prescriptive period to file the same in court is about to expire.

Refund of Unutilised Input Taxes

In the Philippines, sales of goods and services are generally subject to Value Added Tax (VAT) at a regular rate of 12%. This 12% VAT is payable to the tax authority after deducting the input taxes incurred by the taxpayer from its purchases of goods and services.

There are, however, taxpayers whose sales are entitled to VAT at 0%, while their purchases remain subject to the regular 12% VAT rate. This will lead to a scenario where taxpayers accumulate input taxes that may no longer be utilised as credit against available output taxes.

In this case, the law allows the taxpayer to claim for a refund of the unutilised input taxes that are attributable or related to the taxpayer’s VAT zero-rated sales.

Under the law, the taxpayer may file its claim for refund with the tax authority within two years of the close of the taxable quarter when the sales were made. The BIR is given 90 days from filing within which to issue a decision on the taxpayer’s claim. Should the decision be unfavourable to the taxpayer, or remain unacted upon, it may be elevated to the courts within 30 days of the taxpayer’s receipt of the administrative decision, or of the expiry of the 90-day period.

Administrative Denial of Taxpayer’s Request for Confirmatory Rulings

In some cases, taxpayers would ask for clarificatory rulings from the BIR in accordance with the tax authority’s power to interpret the provisions of the Tax Code and other tax laws. If the taxpayer disagrees with the ruling of the tax authority, the ruling may be elevated to the Secretary of Finance for review, and eventually to the courts if the ruling of the Secretary of Finance is adverse to the taxpayer.

On a local level, specifically in cities and municipalities, tax controversies also arise as a result of tax investigations conducted by city or municipal tax authorities, as well as from denials of claims for refund filed with the local tax authorities. The disputes from the local tax authorities may likewise be elevated to the courts.

Court Decisions Confirming Taxability of a Transaction

Court decisions confirming the taxability of certain transactions may lead the tax authority to audit and issue assessments on past transactions not yet covered by prescription. This normally involves industry issues or grey matters that are not clearly defined in tax laws or regulations.

1.2 Causes of Tax Controversies

Generally, tax controversies arise due to taxpayers' poor tax compliance, and complex provisions of tax laws and regulations.

Tax controversies occur in almost all types of taxes, both corporate and individual, such as income tax, VAT, excise tax, donor's tax, estate tax, documentary stamp tax (DST), customs duties, property taxes, withholding tax, and local business taxes. Most of the controversies are in areas of corporate income taxation involving values as high as billions of pesos, due to complex transactions or difficult interpretation of the law.

1.3 Avoidance of Tax Controversies

Tax controversies arising from the tax authority's tax investigations usually occur due to taxpayers' poor tax compliance or difficult interpretation of tax laws as applied to complex transactions. There are many ways to mitigate tax risks arising from audit, such as conducting tax compliance and due diligence reviews every so often, implementing tax education through training and seminars, requesting advance rulings in complex transactions, and receiving professional help and tax advice on new and large transactions. Some companies conduct tax compliance reviews aimed at increasing the level of tax compliance to mitigate tax controversies arising from tax investigation that may be conducted by the tax authority. Some companies that are exposed to related-party transactions conduct transfer-pricing studies, although this is done as part of the regular audit and not a focused transfer pricing audit, considering that transfer pricing in the Philippines has not yet attained maturity.

Tax controversies arising from claims for refunds of unutilised input taxes may possibly be mitigated through strict compliance with the invoicing requirements mandated under the rules. Usually, taxpayers' claims for refund are denied outright as the supporting documents – specifically, the official receipts and invoices supporting the transactions – do not conform with the invoicing requirements under the Tax Code and existing regulations.

1.4 Efforts to Combat Tax Avoidance

The BEPS recommendations and the EU's recent measures to combat tax avoidance have not yet been adopted in Philippine tax laws. However, there is ongoing tax legislation aimed at simplifying and rationalising the tax system in the country, in an effort to increase tax collection and combat tax avoidance.

One such proposed piece of local legislation is the amendment of Section 50 of the Tax Code, to address transfer pricing issues and adopt the "arm's-length principle", which is the internationally accepted standard for determining the appropriate transfer prices for controlled transactions of associated enterprises.

1.5 Additional Tax Assessments

Generally, findings of the tax authority arising from tax investigations are not immediately enforceable. The taxpayer is afforded due process and is given time to refute or appeal the findings of the tax authority, either administratively or with the courts. While the case is being disputed, the taxpayer is not required to pay the amount assessed. Basically, the same procedure is followed in local tax assessments, except in the case of real property taxes, which are required to be paid first under protest before the taxpayer can file a protest. In the case of customs duties, the importer adversely affected by deficiency assessments may likewise appeal administratively and to the courts. Under the new rules of the Customs authority, any importer who has received an audit notification letter may avail of the Bureau of Customs Prior Disclosure Programme by tendering payment of the deficiency duties, taxes and penalties within a period of 90 calendar days from receiving the audit notification letter.

However, in rare instances, the tax authority proceeds with the collection of the assessed taxes by initiating levy and distraint on the taxpayer's properties, even in cases where the tax authority's findings are still being contested and are not yet executory. In situations like this, the taxpayer will have to request the suspension of the collection of tax from the tax court, which is usually granted on the condition of the taxpayer's payment of a bond. In rare cases, though, the tax court grants the suspension of tax collection even without requiring the taxpayer to post a bond.

2. Tax Audits

2.1 Main Rules Determining Tax Audits

As a policy, the tax authority comes out with an audit programme every year that sets the guidelines of who and what taxpayers or industry will be subjected to audit for that year. However, the tax authority can subject any taxpayer it deems necessary to audit, even if it is not covered by the audit programme. Practically, an audit may be conducted on all taxpayers on a yearly basis; the tax authority is not prohibited from doing so. Large taxpayers within the Large Taxpayers Group are subjected to audit almost every year.

In certain instances, however, the BIR conducts targeted audits, as in the case of industry audits, policy or special audits, interrelated company audits or co-ordinated audits involving several taxpayers under different offices of the tax authority.

Ordinarily, the tax authority evaluates the tax payments made by the taxpayer and, if it finds them to be unreasonably low in relation to the taxpayer's assets or net worth or in relation to payments made in the prior years, an audit will most likely be conducted. Furthermore, the tax authority matches a taxpayer's sales against the purchases of its customers; if a discrepancy is revealed, a tax audit will be triggered.

Other factors that usually trigger tax audit are the filing of claims for refund, closure of business, business expansion, and mergers and acquisitions.

2.2 Initiation and Duration of a Tax Audit

Under the law, a tax audit must be conducted within three years of the last day prescribed by law for the filing of the return, or the actual date of filing, whichever is later. This three-year period may be extended if the taxpayer executes a waiver of the defence of prescription in a form prescribed under the rules.

The law does not limit the duration of the audit. The tax investigation may proceed so long as the investigation is conducted within the three-year prescriptive period or within the extended period if the taxpayer executes a waiver of the defence of prescription. However, internal rules of the tax authority require audits to be completed within 120 days of the issuance of the Letter of Authority (LOA), which initiates a tax audit and names certain examiners authorised to conduct it.

2.3 Location and Procedure of Tax Audits

Generally, tax audits must be conducted in the taxpayer's place of business during office hours. However, under the Tax Code, the Commissioner may summon the person or any officer or employee responsible for the payment of the tax to appear before the Commissioner or his or her duly authorised representative to produce books, papers, records, or other data, and to give testimony.

It must be noted though that the Commissioner is not authorised to inquire into bank deposits, except in some cases allowed by law.

The audits are usually based on printed documents or data, although audits based on electronic documents are allowed.

2.4 Areas of Special Attention in Tax Audits

The tax auditors ordinarily pay special attention to the authority given to them in an LOA regarding the coverage of their audit. Their authority to conduct an audit is limited to what is covered in the LOA, and any audit not authorised is considered void. Likewise, an examiner not named in the LOA is not authorised to conduct an audit, and any examination conducted in the absence of a LOA is null and void.

2.5 Impact of Rules Concerning Cross-border Exchanges of Information and Mutual Assistance Between Tax Authorities on Tax Audits

The increasing prevalence of rules concerning cross-border exchanges of information and mutual assistance between tax authorities has, to some extent, increased tax audits, although it is not that significant. Audits that are generally conducted are still the regular audits ordinarily conducted by Philippine tax authorities. As far as is known, no tax audits have been conducted with the tax authorities of different states.

2.6 Strategic Points for Consideration During Tax Audits

During the audit, revenue examiners conduct verification on the taxpayer's business transactions, paying special attention to the day-to-day business operations of the taxpayer, and the manner in which the business transactions are recorded in the taxpayer's books of accounts. In the course of the audit, revenue examiners conduct interviews with not only the officers and staff involved in the accounting processes but also the officers and staff doing operations, marketing and administrative functions.

Transactions with significant amounts or that are considered extraordinary for the line of business of the taxpayer normally attract attention. Also, differences between accounting and tax rules, deferred income tax, related-party transactions, and payments to non-residents are given special attention by auditors.

3. Administrative Litigation

3.1 Administrative Claim Phase

Before initiating a judicial tax case, the administrative phase is mandatory.

Under the current rules, if the revenue examiner finds the taxpayer liable for deficiency taxes, the taxpayer must be notified of the findings. The Tax Code and pertinent regulations require the taxpayer to be informed in writing of the law and the facts on which the assessment is made, or else the assessment is void. An assessment issued not in accordance with this mandate is not binding, and is without force or legal effect.

The taxpayer is required to respond to the final assessments made. If the taxpayer fails to respond, the assessment shall become final and executory.

The assessment may be protested administratively by filing a request for reconsideration or reinvestigation within 30 days of receipt of the assessment, in such form and manner prescribed under the rules. In the cases of motion for reinvestigation, all relevant supporting documents must be

submitted within 60 days from the filing of the protest, or the assessment shall become final. Following the rules, the taxpayer should lodge its protest to the BIR office that has jurisdiction over the taxpayer.

If the protest is denied, in whole or in part, or is not acted upon within 180 days of the submission of documents or the submission of the protest if no subsequent document is submitted, the taxpayer adversely affected by the decision or inaction may appeal to the Court of Tax Appeals (CTA) within 30 days of receiving the decision, or of the lapse of the 180-day period; otherwise, the decision shall become final, executory and demandable.

Note also that if the protest is not acted upon within the 180-day period, the taxpayer may still opt to wait for the tax authority's decision on the protest, and thereafter elevate it to the CTA if the decision on the protest is not favourable to the taxpayer.

A distinction must also be made between decisions made by the Commissioner of Internal Revenue (CIR) and his or her duly authorised representatives, such as the Regional Directors. If a decision (in the form of a Final Decision on Disputed Assessment – “FDDA”) is issued by the Regional Director, a timely motion for reconsideration would suspend the running of the 30-day prescriptive period to appeal to the CTA. On the other hand, if the decision is issued by the CIR, the filing of a motion for reconsideration to him or her will not toll the running of the 30-day prescriptive period to appeal to the CTA.

3.2 Deadline for Administrative Claims

Although the rules suggest that the Commissioner may decide on the taxpayer's protest within 180 days of the taxpayer's submission of supporting documents, the Commissioner does not always issue a decision within this period, and may decide on the protest after the 180 days.

Therefore, in cases where the administrative protest remains unacted upon by the Commissioner within 180 days, the law already allows the taxpayer to appeal the case to the CTA within 30 days of the lapse of the 180-day period. However, failure to elevate the case to the CTA does not render the assessment final and executory; the taxpayer may still opt to wait for the Commissioner's decision on the protest.

4. Judicial Litigation: First Instance

4.1 Initiation of Judicial Tax Litigation

Judicial tax litigation is initiated by filing a Petition for Review with the regular courts or with the Court of Tax Appeals (“CTA”), depending upon the nature and amount involved in the controversy. Local tax cases and national revenue taxes involving amounts of less than PHP1 million

come under the jurisdiction of the regular courts, whereas cases involving more than PHP1 million pesos come under the jurisdiction of the CTA.

In accordance with the Rules of Court of the Philippines, the Petition for Review shall contain, in a methodical and logical form, a plain, concise and direct statement of the ultimate facts of the case. If the defence relied on is based on law, the pertinent provisions of the law and its applicability to the case shall be clearly and concisely stated.

The taxpayer may be represented by a counsel.

4.2 Procedure of Judicial Tax Litigation

Once the Petition for Review is filed, the regular court or the CTA shall issue Summons to the tax authority, requiring the Commissioner to file an Answer to the taxpayer's Petition for Review. Once the Commissioner files an Answer, the tax court shall then schedule the case for a Pre-trial Conference, during which the parties, through counsel, may stipulate the facts both parties agree to be the actual facts surrounding the case. They may likewise agree on issues to be resolved by the Court, and may also agree on the numbers and names of the witnesses, the substance of their testimonies and the approximate number of hours that will be required by the parties for the presentation of their respective witnesses.

Essentially, the Pre-trial Conference aims to narrow down the disputes for the Court's resolution, and to simplify the presentation of evidence.

After the Pre-trial Conference, a series of hearings will be conducted for the presentation of the parties' witnesses and documentary evidence. Once the parties are done presenting their respective witnesses and documentary evidence, the Court shall then direct them to file their respective Memoranda, summarising therein their respective claims and defences.

The Court will decide the case on the basis of the parties' Memoranda and other documents submitted in Court.

4.3 Relevance of Evidence in Judicial Tax Litigation

In judicial tax litigation, testimonial and documentary evidence are relevant as the court decides the case based on the evidence presented by the parties. Witnesses are presented to testify during hearings in open court scheduled for that purpose. During the hearing, the witness will identify and testify on documentary exhibits supporting his testimony.

Under the current rules, testimonies of witnesses are presented in Court through the Judicial Affidavit Rule, under which the Judicial Affidavits of proposed witnesses are filed in Court prior to the scheduled date of hearing, together with the evidentiary documents testified to by the witness.

The Judicial Affidavit already contains the testimony of the witness in a Question and Answer form. Nonetheless, the witness is still required to appear in court for identification of the Judicial Affidavit and the documents identified therein, and to answer cross-examination questions that may be propounded by the opposing party and clarificatory questions that may be asked by the Justices hearing the case.

The documents identified by the witnesses, including their Judicial Affidavits, will be submitted in Court for consideration.

4.4 Burden of Proof in Judicial Tax Litigation

The burden of proof is the duty of a party to present the necessary evidence on the facts in issue to establish his or her claim or defence. The party alleging a fact to be true is initially presumed to be correct, and the burden of proof rests upon the other party. When the party bearing the burden of proof meets its burden, the burden of proof switches to the other party.

In tax controversies, the presumption of regularity is merely disputable, and the burden of proof is shifted to the BIR when the taxpayer denies the allegations.

4.5 Strategic Options in Judicial Tax Litigation

The production of witnesses and documentary evidence takes place during the trial. These documents will eventually be submitted in Court after all witnesses have testified.

Usually, in tax controversies, there are voluminous documents supporting the parties' claims and defences. Thus, the Court usually allows the taxpayer-litigant to present an expert witness who shall conduct an independent audit on the taxpayer's supporting documents, prepare a report and testify thereon.

Under the current rules, the CTA now implements the referral of cases to mediation proceedings, where both the taxpayer and the tax authority may opt to enter into a compromise settlement in order to terminate the tax litigation speedily. Mediation is done before a full-blown case trial.

The parties are not obliged to settle but are merely referred to a mediation centre to discuss the possibility of entering into mediation. Either of them may refuse. If either the taxpayer or the tax authority is not willing to enter into mediation, the mediation proceedings would be terminated and the trial proceedings will continue. If the mediation is successful, it may result in either a full or partial compromise. A full compromise would terminate the litigation proceedings, but a trial will continue on the remaining issues if there is only a partial compromise.

4.6 Relevance of Jurisprudence and Guidelines to Judicial Tax Litigation

Court decisions are generally based on local tax laws and regulations – primarily the Tax Code. However, in the absence of local laws and regulations applicable to a certain issue at hand, the Courts may consider jurisprudence in other jurisdictions. Jurisprudence and laws in foreign jurisdictions have persuasive legal effect in the Philippines, consistent with the State's policy that generally accepted principles of international law are adopted as part of the laws of the land.

5. Judicial Litigation: Appeals

5.1 System for Appealing Judicial Tax Litigation

Appealing judicial tax litigation depends upon the nature and value of the dispute involved. If the controversy arises from local tax issues or national revenue taxes where the amount involved is less than PHP1 million, the case comes under the jurisdiction of the regular courts, whereas if the amount involved is at least PHP1 million, the jurisdiction lies with the CTA.

In a judicial appeal, the litigant is not allowed to commence or file any other request or proceeding involving the same subject-matter or issues in another tribunal. In an unfavourable decision, however, the adverse party is given several opportunities to appeal the case by filing a motion for reconsideration in the same tribunal, and later elevating the case to a higher tribunal until it reaches the Supreme Court.

5.2 Stages in the Tax Appeal Procedure

In tax controversies, the Petition for Review is filed with the CTA Division or with the regular courts, depending upon the nature and amount involved in the controversy.

For cases under the original jurisdiction of the CTA, the CTA Division shall conduct the trial of the case, where party litigants are given opportunities to present witnesses and documentary evidence supporting their respective claims. The Court shall promulgate a Decision on the basis of the evidence submitted by the parties. Once a Decision is promulgated, the aggrieved party may file an appeal by way of a Motion for Reconsideration (MR) or a Motion for New Trial (MNT) before the same Division. If no MR or MNT is filed, the Decision of the CTA Division shall become final and executory.

Based on its merits, the CTA Division may grant or deny the MR or MNT. The aggrieved may then appeal to the CTA En Banc, which may sustain, reverse or modify the Decision of the CTA Division. If the Decision of the CTA Division is not elevated to the CTA En banc, it shall become final and executory.

The aggrieved party may appeal the Decision of the CTA En Banc by way of a Motion for Reconsideration to the same Court, which may be denied or granted, depending upon its merits. If no MR is filed before the CTA En banc, the Decision shall become final and executory.

The aggrieved party may then appeal the decision of the CTA En Banc to the Supreme Court. The Decision of the Supreme Court is final.

A full-blown trial is likewise conducted in the regular courts for cases under their jurisdictions. During the trial, the parties are given ample time to present their side of the case by presenting witnesses and documentary evidence supporting their respective claims. The regular court shall promulgate a decision on the basis of the evidence submitted by the parties. An aggrieved party may file an MR, and later elevate the case to the CTA, and all the way to the Supreme Court.

5.3 Judges and Decisions in Tax Appeals

Regular Courts

In a regular court, only one presiding judge is assigned, who is appointed by the President of the Philippines. Cases under the jurisdiction of the regular courts include local tax cases and national internal revenue taxes involving claims of less than PHP1 million.

The Court of Tax Appeals

The Court of Tax Appeals is composed of a Presiding Justice and eight Associate Justices, likewise appointed by the President of the Philippines. In appropriate cases, the Court shall sit en banc, or in three Divisions of three justices each, including the Presiding Justice, who shall be the Chairman of the First Division.

Cases in Divisions are heard and decided upon by three Associate Justices sitting as one body. The chairman of the Division or, in his or her absence, its senior member shall preside over the sessions of the Court in Divisions. The attendance of at least two justices of the Court shall be necessary to constitute a quorum for its sessions in Divisions. The presence at the deliberation and the affirmative vote of at least two justices shall be required for the pronouncement of a judgment or final resolution of the Court in Divisions.

Cases within the jurisdiction of the Court in Divisions include reviews of Decisions of the CIR in cases involving disputed assessments, refunds of internal revenue taxes, fees or other charges, or other matters arising under the National Internal Revenue Code, as amended, or other laws administered by the BIR.

Cases in CTA En Banc are decided upon by the eight Associate Justices and the Presiding Justice sitting as one body. The presiding justice or, in his or her absence, the most senior justice in attendance shall preside over the sessions of the

Court en banc. The attendance of five justices of the Court shall constitute a quorum for its sessions en banc. The presence at the deliberation and the affirmative vote of five justices of the Court en banc shall be necessary for the rendition of a decision or resolution on any case or matter submitted for its consideration. Where the necessary majority vote cannot be had, the petition shall be dismissed; in appealed cases, the judgment or order appealed against shall stand affirmed; on all incidental matters, the petition or motion shall be denied.

The CTA en banc exercises exclusive appellate jurisdiction to review by appeal Decisions or Resolutions of the Court in Divisions as well as Decisions, Resolutions or Orders of the Regional Trial Courts in local tax cases decided or resolved by them in the exercise of their appellate jurisdiction, among others.

The Supreme Court

The Supreme Court is composed of a Chief Justice and 14 Associate Justices, likewise appointed by the President of the Philippines. It may sit en banc or, at its discretion, in divisions of three, five or seven members.

Cases heard by the Supreme Court en banc includes cases involving the constitutionality of a treaty, international or executive agreement, and the constitutionality of presidential decrees, proclamations, orders and instructions, among others.

6. Alternative Dispute Resolution (ADR) Mechanisms

6.1 Mechanisms for Tax-related ADR in this Jurisdiction

Under the current rules of the CTA, the tax authority and the taxpayer may now undergo mediation proceedings, during which they are given an opportunity to enter into a compromise settlement that aims to expedite the disposition of the case. The compromise agreement shall be in accordance with the terms and conditions set forth under the Tax Code.

If no compromise settlement is agreed upon during the mediation proceedings, the case will then proceed to trial. However, at any time during the proceedings and while the case is pending decision, the parties may still enter into a compromise agreement, in accordance with the terms and conditions allowed under the Tax Code.

6.2 Settlement of Tax Disputes by Means of ADR

Under the rules on mediation currently being implemented by the CTA, parties to a dispute are to undergo mediation proceedings before the Court proceeds with the trial of the case. During the mediation hearing, the parties will be asked of their willingness to undergo mediation and explore a compromise settlement.

If the parties manifest their opposition to mediation proceedings, the mediation will be terminated right away and the Court shall proceed with the trial of the case.

6.3 Agreements to Reduce Tax Assessments, Interest or Penalties

As it stands now, the compromise agreement shall be subject to the conditions set forth under the Tax Code, as follows:

- a reasonable doubt as to the validity of the claim against the taxpayer exists; or
- the financial position of the taxpayer demonstrates a clear inability to pay the assessed tax.

The compromise settlement of any tax liability shall be subject to the following minimum amounts:

- for cases of financial incapacity, a minimum compromise rate equivalent to 10% of the basic assessed tax; and
- for other cases, a minimum compromise rate equivalent to 40% of the basic assessed tax.

Where the basic tax involved exceeds PHP1 million, or where the settlement offered is less than the prescribed minimum rates, the compromise shall be subject to the approval of the Evaluation Board, which shall be composed of the Commissioner and the four Deputy Commissioners.

6.4 Avoiding Disputes by Means of Binding Advance Information and Ruling Requests

Rulings duly issued by the tax authority effectively help in avoiding disputes between the tax authority and the taxpayers. Thus, in cases where there are issues concerning the interpretation of tax laws and regulations relative to the taxability of certain transactions, taxpayers normally resort to requesting confirmatory rulings from the BIR for their guidance.

6.5 Further Particulars Concerning Tax ADR Mechanisms

If the parties are willing to undergo mediation proceedings, they will select a mediator from among the list of mediators accredited by the CTA. If the parties fail to choose their mediator/s, the Chairperson of the Philippine Mediation Centre (PMC) shall choose the mediator/s for the parties, in accordance with the guidelines of the Philippine Mediation Centre Office (PMCO). The Mediator selected by the parties may decline the appointment or ask to be relieved on the grounds of actual or perceived conflict of interest, or any other valid grounds, subject to the approval of the Chairperson.

The parties themselves may appear during the mediation proceedings, although the taxpayer may be represented by a counsel, if he or she so desires. Duly authorised representatives of private parties shall be required to file a special power

of attorney (SPA) with the PMC in favour of an officer/s, showing their full authority, including but not limited to the powers to appear in representation of the party, to enter into stipulations of facts and to offer, negotiate, accept, decide, and enter into a compromise agreement that will put an end to the litigation. In the case of corporate parties, said authority must be in the form of a board resolution or secretary's certificate.

The representatives of the BIR shall be required to file the appropriate SPA issued by the CIR or COC or their duly Authorised Officials with the PMC.

The mediation proceedings may take place in the premises of the court or in another venue as may be agreed upon by the parties.

6.6 Use of ADR in Transfer Pricing and Cases of Indirect Determination of Tax

At the moment, transfer-pricing rules are not strictly implemented in the Philippines, but in cases where transfer-pricing issues are raised or assessed through regular audits, the same rules as for regular cases apply. Thus, there are no special ADR mechanisms in transfer-pricing cases.

7. Administrative and Criminal Tax Offences

7.1 Interaction of Tax Assessments with Tax Infringements

In cases where correct taxes were not properly paid, the taxpayer is charged with surcharge and interest as civil penalties. However, this does not automatically subject the taxpayer to a criminal offence. In various decisions of the Court of Tax Appeals and the Supreme Court, it has been held that a deliberate intent to evade tax or defeat tax must be proved in order to establish the taxpayer's criminal liabilities.

7.2 Relationship Between Administrative and Criminal Processes

In cases within the jurisdiction of the CTA, the criminal action and the corresponding civil action for the recovery of civil liability for taxes and penalties shall be deemed jointly instituted in the same proceeding. The filing of the criminal action shall necessarily carry with it the filing of the civil action. No right to reserve the filing of such civil action separately from the criminal action shall be allowed or recognised.

7.3 Initiation of Administrative Processes and Criminal Cases

An administrative infringement process does not necessarily evolve into a criminal tax case. Pursuant to the Run Against Tax Evaders (RATE) Programme of the government, the institution of criminal cases against tax evaders

has increased in recent years. Under the RATE programme, the BIR is mandated to investigate criminal violations of the National Internal Revenue Code of 1997, as amended, and to assist in the prosecution of criminal cases that will generate the maximum deterrent effect, enhance voluntary compliance, and promote public confidence in the tax system.

7.4 Stages of Administrative Processes and Criminal Cases

Criminal tax cases are initially filed at the Department of Justice for the determination of probable cause. Once probable cause is determined to exist, the case will then be filed either at the regular court or at the Court of Tax Appeals, depending on the amount involved in the case.

In the CTA, all criminal actions before the Court in Division in the exercise of its original jurisdiction shall be instituted by the filing of information in the name of the People of the Philippines. In criminal actions involving violations of the Tax Code and other laws enforced by the BIR, the CIR must approve their filing. In criminal actions involving violations of the Tariff and Customs Code and other laws enforced by the BOC, the Commissioner of Customs must approve their filing.

The institution of a criminal action shall interrupt the running of the period of prescription.

All criminal actions shall be conducted and prosecuted under the direction and control of the public prosecutor, the Office of the Solicitor General. In criminal actions involving violations of the Tax Code and other laws enforced by the BIR, and violations of the Tariff and Customs Code or other laws enforced by the BOC, the prosecution may be conducted by the respective duly deputised legal officers.

7.5 Possibility of Fine Reductions

Upfront payment of the additional tax assessment does not necessarily entitle the taxpayer to reductions of potential fines applicable to the offence committed. Fines and penalties arising from criminal actions are specifically stated in the Tax Code and other tax laws.

7.6 Possibility of Agreements to Prevent Trial

Payment of the tax assessed plus interest and penalties does not ordinarily prevent or stop a criminal tax trial. There are certain instances, however, where the tax authorities agreed to compromise, dropping the criminal aspect if the civil liability is paid. Normally, this is resorted to by the tax authorities if their evidence to convict the taxpayer is weak, or if the amount to be paid is substantial. In a recent case involving unpaid excise taxes, the Commissioner agreed to a settlement of over PHP30 billion in exchange for dropping the criminal case.

Such settlement may also happen at the prosecutor's office but with the agreement of the Commissioner. Under the CTA rules on mediation, cases arising from criminal offences within the jurisdiction of the Court En Banc or in Divisions are not covered by mediation.

7.7 Appeals Against Criminal Tax Decisions

An appeal to the CTA in criminal cases decided by a regular court in the exercise of its original jurisdiction shall be taken by filing a notice of appeal within 15 days of receiving a copy of the decision or final order with the court that rendered the final judgment or order appealed against, and by serving a copy upon the adverse party. The Court in Division shall act on the appeal.

An appeal to the Court en banc in criminal cases decided by the Court in Division shall be taken by filing a petition for review within 15 days of receiving a copy of the decision or resolution appealed against. The Court may, for good cause, extend the time for filing the petition for review for an additional period not exceeding 15 days.

An appeal to the Court in criminal cases decided by the Regional Trial Courts in the exercise of their appellate jurisdiction shall be taken by filing a petition for review within 15 days of receiving a copy of the decision or final order appealed against. The Court en banc shall act on the appeal.

7.8 Rules Challenging Transactions and Operations in this Jurisdiction

Several transfer-pricing issues have been raised to the court, but no transfer-pricing case has yet won in the Supreme Court.

8. Cross-border Tax Disputes

8.1 Mechanisms to Deal with Double Taxation

If a double-taxation situation occurs due to an additional tax assessment or tax adjustment in a cross-border situation, domestic litigation is often resorted to against such administrative decision.

8.2 Application of GAAR/SAAR to Cross-border Situations

The GAAR or SAAR is not adopted in the Philippines.

8.3 Challenges to International Transfer Pricing Adjustments

In the Philippines, no international transfer-pricing adjustments have been challenged under domestic tax courts.

8.4 Unilateral/Bilateral Advance Pricing Agreements

Unilateral or bilateral advance pricing agreements (APAs) are recognised under the BIR's Transfer Pricing regulations

as a mechanism to eliminate double taxation issues arising from transfer-pricing adjustments. However, the Bureau has yet to issue implementing guidelines.

APAs are not adopted as a mechanism to avoid or mitigate litigation in transfer-pricing matters.

8.5 Litigation Relating to Cross-border Situations

Currently, withholding tax and Permanent Establishment are the primary issues in litigation relating to cross-border situations. Requests for confirmatory rulings with the tax authority could mitigate such litigation.

9. Costs/Fees

9.1 Costs/Fees Relating to Administrative Litigation

No filing fee is required in instituting tax cases at the administrative level. The costs or fees that may possibly be associated with tax controversy are limited to actual expenses incurred in pursuing the administrative case, such as professional fees, time spent, and other logistical expenses.

9.2 Judicial Court Fees

The filing fee in instituting cases with the CTA is approximately 1% of the amount involved. The filing fee shall be paid by the taxpayer with the court upon filing the Petition for Review. A minimal amount of the filing fee shall also be paid by the taxpayer upon appeal of the case to the CTA En Banc, as well as to the Supreme Court.

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9.3 Indemnities

The taxpayer is not awarded any type of indemnity if the court decides that the initial additional tax assessment is absolutely void and null. The filing fee is a sunk cost of the taxpayer filing the appeal in court.

9.4 Costs of Alternative Dispute Resolution

If the parties decide to proceed with mediation proceedings, the mediator shall be entitled to PHP2,500 as the basic mediator's fee, regardless of the outcome of the mediation. Upon the Court's approval of the signed compromise agreement, the mediator shall be entitled to additional remuneration up to a maximum amount of PHP50,000, depending on the amount involved in the controversy.

10. Statistics

10.1 Pending Tax Court Cases

There is no exact data regarding the number of pending tax court cases, including those pending in the regular courts. At the time of writing, however, more than 10,000 tax cases have already been filed with the CTA Divisions. Values are as high as billions of pesos per case, although there are also cases filed in court that involve only a small amount of tax deficiencies.

10.2 Cases Relating to Different Taxes

There is no readily available data regarding the number of cases initiated and terminated every year relating to different taxes, such as corporate income tax, individual income tax, VAT, customs duties, stamp duties, transfer tax, and others.

10.3 Parties Succeeding in Litigation

There is no readily available data on which party (tax authorities or taxpayers) succeeds in litigation.

11. Strategies

11.1 Strategic Guidelines in Tax Controversies

Strategic guidelines to consider in a tax controversy would depend upon the nature, issues and amount of the case in question.