



## AN ASSESSMENT OF RA 9504

By:

**Director Erlinda R. Aguja**



Republic Act No. 9504 which was passed on June 17, 2008 amended Sections 22, 24, 34, 35, 51 and 79 of RA 8424, as amended otherwise known as the National Internal Revenue Code of 1997. This piece of legislation was basically intended to provide economic relief to individual taxpayers, particularly the minimum wage earners. Thus, apart from the uniform grant of a higher personal exemptions of P50,000 to individual taxpayers and P25,000 to each qualified dependent not exceeding four dependents, those earning the statutory minimum wage in the private sector and likewise those in the public sector with equivalent compensation in the non-agricultural sector where he/she is assigned are made exempt from the income tax. Holiday pay, hazard pay, overtime pay and night differential pay received by these minimum wage earners are likewise exempt from the tax. As such, the filing and withholding of tax required prior thereto are abolished. The issuance of the implementing rules and regulations (RR 10-2008) by the BIR was considerably delayed on account of the clamor for the full year application of the tax exemption and the upgraded amounts of personal exemptions instead of just half year of 2008, considering that the law was enacted only in June

2008. Legislators were one in insisting that the intent of the law was for a full year application, it being a tax relief measure. Petitions were filed in court to uphold the full year application, in the light of earlier decisions on similar cases in the past.

Consequently, this tax relief package was initially estimated to cost the national coffers P14.25 Billion. (The Dept. of Finance recently estimated the revenue loss to have reached a whopping P26.0 Billion<sup>1</sup>). To mitigate therefore, the attendant revenue drain, RA 9504 included the grant of a 40% optional standard deduction (OSD) based on gross sales/receipts to self-employed and professionals and 40% OSD for corporations based on their gross income. The Department of Finance (DOF) estimated that with the probable shift to the OSD system by a certain percentage of these taxpayers who were then itemizing their deductions, an estimated P15.03 Billion in additional revenue will be realized thereby offsetting the loss from the tax relief package. In short, a revenue gain was expected to ensue. It should be noted however, that no curtailment of the deductible expenses under Section 34 of the Tax Code was made, hence the option to itemize deduction remained. Earlier, the House version aimed for the introduction of the Simplified Net Income Tax Scheme (SNITS) for both individuals and corporation along with the modified OSD scheme. Unfortunately, only the OSD scheme was

carried in the enacted law. Significant revenue shortages were alluded to the erosive nature of RA 9504 and proposals to finally adopt the SNITS were filed to address its failure to meet the revenue expectations. There are also moves to once again restructure the income tax rates of both individuals and corporations to make the tax more progressive

and revenue productive.

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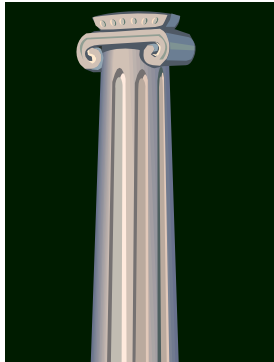
<sup>1</sup> Maria Fe V. Mendoza et al. (editors), *Economic Reforms for Philippine Competitiveness* published by the University of the Philippines Open University: 2010 p9.

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## WHY CREATE A PHILIPPINE TAX AND TARIFF ACADEMY?

By:

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Taxes are the lifeblood of a country. They are used to run the entire government bureaucracy, namely: to pay for the salaries of our civil servants, i.e., public school teachers, police, armed forces, etc.; build infrastructures like roads and bridges; support the Local Government Units (LGUs) through Internal Revenue Allotment (IRA<sup>1</sup>), among others.

Therefore taxation is a very important power of the state to generate revenues to be able for the government to provide the basic goods and services and ultimately improve the standard of living of our people. However, we have overlooked the very important aspect of improving our tax collection through enhancement of human resources by providing appropriate education, technical training, skills, and formation of values through a specialized training academy for tax collectors and administrators. Our tax collectors and administrators have a critical role in meeting their targets of generating needed revenues for the country's total development. For instance, for

the year 2010, our tax collectors/administrators have been mandated to collect P800 Billions of taxes to fund the budget.

It is from this perspective that the Congress of the Philippines, i.e., the Philippine Senate and the House of Representatives have deemed it urgent to pass this bill<sup>2</sup> creating the Philippine Tax and Tariff Academy.

It is worthy to note that we have many institutions or academies aimed at providing specialized trainings such as:

- Judicial Academy<sup>3</sup> which serves as a training school for justices, court personnel, lawyers and aspirants to judicial posts and it is under the umbrella of the Supreme Court.

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<sup>1</sup> Forty percent (40%) of BIR collection is allocated as IRA for LGUs.

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<sup>2</sup> Senate Bill No. 3206, entitled: "An Act Creating the Philippines Tax Academy, Defining its Powers and Functions, Appropriating Funds Therefore and for Other Purposes, authored by Senator Panfilo Lacson; and House Bill No. 7134 (Committee Report No. 2590), entitled: "An Act Establishing the Philippine Tax Academy, Defining its Powers and Functions" authored by Reps Exequiel B. Javier, Eduardo R. Gullas and Alfonso V. Umali, Jr.

<sup>3</sup> Created by RA 8557 entitled: "An Act Establishing the Philippine Judicial Academy, Defining Its Powers and Functions, Appropriating Funds Therefore, and For Other Purposes" dated February 26, 1998.

- Philippine Military Academy (PMA)<sup>4</sup> which serves as a military training school for selected cadets of the Armed Forces of the Philippines.
- Philippine National Police Academy (PNPA)<sup>5</sup> which provides training/education for the Philippine National Police.
- Local Executive Academy (LEA)<sup>6</sup> which serves as a training and development institute for local government officials and personnel of the Department of Interior and Local Government.

We also have many universities and colleges that have been offering academic medical courses, seminars, and training programs in almost all fields of expertise (e.g. medical care and nursing, engineering, architecture, education, economics, finance, tourism, hotel and restaurant management, business administration, airline administration, etc. but not a single course is even remotely related to tax administration.

A number of neighboring countries e.g., Japan, Korea, Malaysia, India, and China have built their own tax academies/colleges for the purpose of raising the professional competency and standards of their tax community and providing tax education to the public apart from their tax practitioners.

Malacanang even recognizing the urgency of passing the bill, hence, it has certified on February 1, 2010 the necessity of the immediate enactment of this bill to address the critical need to provide tax collectors and administrators with relevant education, training, and skills to further improve their tax collection efficiency and competence as public servants.

Congress believes that at present there is no need to legislate for new taxes. Rather a paramount importance in the short and long-term is that of focusing government effort and resources to build competent, efficient, and honest workforce in the area of tax collection and administration.

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*Note: At least One Million Pesos tax money is expended for one PMA cadet. Thus, the state should really invest for the education/training of our tax collectors and administrators.*

**– Q & A –**

*1) What is withholding tax on compensation?*

Withholding tax on compensation is a kind of withholding tax imposed on income payments to individuals receiving purely compensation income arising from an employer-employee relationship which is creditable against the income tax due of the employee for the taxable year but does not constitute full and final payment of the income tax due from the employee on the said income.

*2) What is value-added tax?*

Value-added tax is a tax on the sale, barter, exchange, lease of goods and properties, rendition of services, and importation of goods.

Source: Tax Calendar, BIR 2010  
 Making the Public Know

<sup>4</sup> Created by Commonwealth Act No. 1 entitled: "An Act to Provide for the National Defense of the Philippines, Penalizing Certain Violations Therefore, Appropriating Funds Therefore, and For Other Purposes".

<sup>5</sup> Created by PD 1184 entitled: "Integrated National Police Personnel Professionalization Law of 1977".

<sup>6</sup> Created by EO No. 262 entitled: "Reorganizing the Department of Local Government and For Other Purposes".

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## ASSESSMENT OF RA NO. 10026

By:

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### Salient Features

Republic Act (RA) No. 10026 entitled “An Act Granting Income Tax Exemption to Local Water Districts by Amending Section 27(C) of the National Internal Revenue Code (NIRC) of 1997, as Amended, and Adding Section 289-A to

the Code for the Purpose” lapsed into law on March 11, 2010. It was published in Business Insights and Manila Standard Today on March 29, 2010. The law exempted local water districts (LWD) all over the country from the corporate income tax. The LWDs’ income tax liabilities, reckoned from 13 August 1996 up to the effectivity of the Act, have also been condoned, thereby making the tax exemption retroactive.

In exchange for the tax privilege, LWDs are required to channel the amounts, hitherto uncollected by the Bureau of Internal Revenue (BIR), to capital equipment expenditure in order to expand water service coverage and to improve water quality.

### Historical Background

The original charter of LWDs, Presidential Decree (PD) No. 198, declared as an objective of national policy with high priority “the creation, operation, maintenance and expansion of reliable and economically viable and sound water supply and wastewater disposal system for population centers of the Philippines” through independent, locally controlled public water districts. To achieve this objective, LWDs were exempted from income tax, and all National Government, local government and municipal taxes and fees (including any franchise, filing, recordation, license

or permit fees, or taxes and fees, charges or costs involved in any court of administrative proceeding), and all duties or imposts on imported machinery, equipment and materials required for their operations.

Over time, however, the tax exemption privileges were withdrawn (under Executive Order No. 93), then restored for a limited 5-year period (under RA No. 7109).

On the issue of a public utility, the LWDs were also subjected to adverse rulings by the BIR. It maintained that LWDs are subject to the corporate income tax because they are “not composite of the National Government or its political subdivision performing essential government function” (BIR Ruling No. 074-98 dated May 27, 1998 and BIR Revenue Memorandum Circular No. 63-2003 dated October 10, 2003). On the other hand, the BIR ruled that the Metropolitan Waterworks and Sewerage System (MWSS) and National Power Corporation (NPC) are public utilities, hence, exempt from the income tax (BIR Ruling DA 088-2001 dated May 16, 2001 and BIR Ruling No. 018-2000 dated January 20, 2000, respectively).

Meanwhile in Case No. OSJ-2005-03 the Department of Justice (DoJ) ruled that it does not see rational basis in exempting PAGCOR and PCSO vis-à-vis LWDs from income tax where one proceeds from gambling while the other proceeds from basic necessity. The DoJ said that if BIR “can exempt MWSS there is no reason why it cannot exempt the water districts all over the country. There is no reason why a huge company can be exempt while a small entity cannot be exempt”.

### Assessment

RA No. 10026 therefore corrected all differences in the interpretation of the tax regime

for LWDs by exempting their income from the corporate income tax and by condoning all income tax liabilities reckoned from 13 August 1996 up to the effectivity of the Act.

The landmark legislation, principally authored by Senators Lacson and Escudero, would enable all LWDs to pursue its mandate to acquire, install, improve, maintain and operate water supply and distribution systems for domestic, industrial, municipal and agricultural uses for residents and lands within the boundaries of such districts, and to provide, maintain and operate wastewater collection, treatment and disposal facilities therein.

The requirement under Section 2 of the Act for LWDs to adopt internal control reforms intends to ensure their economic and financial viability. As non-stock and non-profit corporations, LWDs receive no government subsidy and they are not included in the National Government budget (GAA). Their operations are basically sourced from internally-generated funds and loans from the Local Water Utilities Administration (LWUA), local and foreign sources.

As a safeguard against unscrupulous spending, the law also restricts LWDs from increasing by more than twenty percent (20%) their annual appropriation for personal services, travel, transportation or representation expenses, as well as the purchase of motor vehicles. This condition was imposed so that “savings” or the amount that should have been paid as income tax would be plowed back to the operations and capital equipment expenditure.

To further ensure that the intent of the law is achieved, all LWDs – through the LWUA – are required to submit to the Committee on Ways and Means of both Houses of Congress, statistical data and financial statements which shall show how the funds are utilized and the internal reforms implemented. These data shall be used by Congress in evaluating the faithful compliance to the conditions set forth under RA No. 10026 and serve as basis for the continued enjoyment of the tax privilege or its termination, as the case may be.

**FACTS:**

In the case of Cabili vs CSC, GR No. 156503, June 22, 2006, the Supreme Court ruled that water districts are government-owned and –controlled corporations with original charters created pursuant to PD 198. Hence, they are under the jurisdiction of the CSC.

In Marilao Water Consumers Association vs IAC, GR No. 72807, Sept. 9, 1991, the highest tribunal said “LWUA does not appear to have adjudication powers over local water districts”. LWUA is primarily a specialized lending institution for the promotion, development, and financing of local water utilities with power to prescribe minimum standards and regulations regarding maintenance; operation; personnel training, accounting and fiscal practices for local water utilities; to furnish technical assistance and personal training programs therefor; monitor and evaluate local water standards; and effect systems integration, joint investment and operations, district annexation and deannexation whenever economically warranted. LWUA has quasi-judicial power only as regards rates or charges fixed by water districts, which it may review to establish compliance with the provisions of PD 198, without prejudice to appeal being taken therefrom by a water concessionaire to the National Water Resources Council whose decision thereon shall be appealable to the Office of the President.

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