May 19, 2021

BIR RULING NO. VAT-173-21

Secs. 28 (B) (1); 42 (C) (3); & 108, NIRC;
BIR Ruling No. 297-11

Anti-Money Laundering Council
Room 507, 5/F, EDPC Building, Bangko Sentral ng Pilipinas Complex
Malate, Manila

Attention: *Mr. Mel Georgie B. Racela*
Executive Director

Gentlemen :

This refers to your letter dated July 13, 2020 requesting confirmation that payments to **AAA** (the "Consultant"), a non-resident, foreign service provider, for services rendered outside the Philippines are not subject to Philippine income tax, and consequently, to the withholding tax and value-added tax (VAT).

Background

1. The Consultant is a _____ resident, with office address at _____.

2. The Philippines underwent the Third Round Mutual Evaluation (ME) [1] process in 2018 to 2019. Based on the ME results, the Philippines meet the ICRG [2] referral criteria. Jurisdictions who meet the criteria enter a twelve (12)-month observation period. The 12-month observation period, which started in October 2019, is an opportunity for the Philippines to remedy the identified shortcomings in the ME report.

3. On June 10, 2020, the Anti-Money Laundering Council (AMLC) entered into a Consultancy Agreement [3] with the Consultant, wherein it was agreed that the following services are to be provided:

"1. Nature of Services

1.1. The Consultant shall provide strategic Anti-Money

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Laundering/Counter-Terrorism Financing (AML/CTF) expertise and technical advice to the AMLC in support of the International Cooperation Review Group (ICRG) process, the Twelve-month Observation Period and overall improvements to the Philippines' AML/CTF system in line with the Financial Action Task Force (FATF) Standards.

1.2. Services will be provided both through desk-based review and in-country missions, as broadly agreed by the Parties, and in accordance with the Terms of Reference (TOR) (Annex A), which is made an integral part hereof.

1.3. Conference calls and email communications shall take place to plan, coordinate and discuss the tasks being carried out by the Consultant and the relevant government ministries and agencies of the Philippines and in line with the demand from the project."

4. The Consultancy Services Agreement is valid for a period of nine (9) months, starting June 10, 2020 and ends on February 28, 2021, renewable at the option of the AMLC, subject to the execution of another Agreement. The main outputs of the consultant will be the inputs on the reports and documents relative to the ME Post Observation requirements. Guidance and advice can likewise be delivered through emails and conference calls. Workshops are conducted to assist the Philippines in organizing and writing reports. [4]

5. Given the global pandemic, all the services are rendered outside of the Philippines such as the desk-based reviews and the in-country missions/workshops which shall be delivered online or remotely.

In reply, please be informed that Sections 23 (D) and 25 (B) of the National Internal Revenue Code of 1997, as amended (Tax Code) provide:

"SEC. 23. General Principles of Income Taxation in the Philippines. — *Except when otherwise provided in this Code:*

xxx xxx xxx

(D) An alien individual, whether a resident or not of the Philippines, is taxable only on income derived from sources within the Philippines;"

"SEC. 25. Tax on Nonresident Alien Individual. —

xxx xxx xxx

(B) Nonresident Alien Individual Not Engaged in Trade or Business within the Philippines. — There shall be levied, collected and paid for each taxable year upon the

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entire income received from all sources within the Philippines by every nonresident alien individual not engaged in trade or business within the Philippines as . . . salaries, wages, . . . compensation, remuneration, . . . a tax equal to twenty-five percent (25%) of such income. . . ."

In relation to the above provisions, Section 42 (A) (3) and (C) (3) of the Tax Code states that compensation for labor or personal services is derived from sources within the Philippines if the services are performed therein, and outside if the services are performed outside the Philippines, to wit:

"SEC. 42. Income from Sources within the Philippines. *—*

(A) Gross Income from Sources within the Philippines. — The following items of gross income shall be treated as gross income from sources within the Philippines:

xxx xxx xxx

(3) Services. — Compensation for labor or personal services performed in the Philippines;

xxx xxx xxx

(C) Gross Income from Sources without the Philippines. — The following items of gross income shall be treated as income from sources without the Philippines:

xxx xxx xxx

(3) Compensation for labor or personal services performed without the Philippines;"

Pursuant to the above provisions, non-resident alien individuals are subject to income tax only on income derived from all sources within the Philippines. Conversely, they are not subject to income tax on income derived from sources outside the Philippines.

This Office explained in BIR Ruling No. 212-12 dated March 23, 2012:

"The situs of tax for services is the place where the service is rendered. Under the Philippine source of income rules for income tax purposes, service income will be considered Philippine source income only if the services are rendered in the Philippines. Conversely, if the services are rendered outside the Philippines, the service income will be considered as foreign source income. x x x

"The rule in this jurisdiction regarding tax situs is: the source of an income is the property, activity or service that produced the income; the test of taxability is the

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source, and the source of an income is that activity which produced the income (CIR v. British Overseas Airways Corporation, G.R. Nos. 65773-74, April 30, 1987). Stated differently, ***the situs of the income derived from labor or personal services is determined solely by the place where service is rendered*** *(CIR v. Japan Airlines, Inc., G.R. No. 60714, March 6, 1991).* ***Compensation from services performed abroad is, therefore, considered income from sources without the Philippines and thus not subject to Philippine income tax****."* (Emphasis supplied.)

Applying the foregoing provisions, since **AAA** is a non-resident alien individual not doing business in the Philippines and her professional fees or compensation constitute income derived from sources outside the Philippines, it can be said that the same are not subject to income tax, and consequently, to the withholding tax.

On the other hand, Section 108 (A) of the Tax Code clearly reads that the sale or exchange of services subject to VAT include only those services that are performed in the Philippines, *viz.*:

> **"SEC. 108. Value-Added Tax on Sale of Services and Use or Lease of Properties**. —
>
> **(A) Rate and Base of Tax**. — There shall be levied, assessed and collected, a value-added tax equivalent to twelve percent (12%) of gross receipts derived from the sale or exchange of services, including the use or lease of properties.
>
> The phrase 'sale or exchange of services' means the performance of all kinds of services in the Philippines for others for a fee, remuneration of consideration. . ."

Accordingly, the service fees to be paid by **AMLC** to **AAA**, to the extent that the subject services are not performed in the Philippines, are exempt from VAT.

IN VIEW OF THE FOREGOING, this Office hereby CONFIRMS your opinion that the income payments made for services rendered abroad or outside the Philippines by **AAA** to **AMLC** are NOT subject to Philippine income tax, withholding tax, and VAT.

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

Very truly yours,

(SGD.) CAESAR R. DULAY

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Footnotes

1. The ME is a mechanism to determine a jurisdiction's level of compliance with international Anti-Money Laundering and Combatting the Financing of Terrorism (AML/CFT) standards.
2. The ICRG is a mechanism of the Financial Action Task Force (FATF) to identify and respond to jurisdictions with strategic deficiencies in their AML/CFT regimes that pose a risk to the international financial system and impede efforts to money laundering and terrorist financing.
3. Refer to Consultancy Services Agreement between AMLC and AAA dated June 11, 2020.
4. See Terms of Reference particularly Item E on Timelines/Deliverables.

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