November 16, 2018

BIR RULING NO. 1366-18

Sections 33 & 34, 1997 NIRC; Revenue Regulations No. 3-98; BIR Ruling No. DA-152-07

Nestlé Philippines, Inc.
Nestlé Center, 31 Plaza Drive
Rockwell Center
Makati City

Attention: *AAA*

Gentlemen :

This refers to your letter dated February 22, 2017 requesting for a ruling on the tax treatment of the issuance of shares or cash equivalent received by the eligible employees of **NESTLÉ PHILIPPINES, INC. (NPI)** from the **Company's Performance Share Unit Plan (PSUP)**.

It is represented that NPI is a corporation organized under the laws of the Philippines on May 23, 1961 with principal office in Cabuyao, Laguna. It is a wholly-owned subsidiary of Nestlé S.A., a company organized under the laws of Switzerland. The Company is primarily engaged in the manufacture and distribution of food and beverage products. NPI maintains an administrative office in Makati City.

It is likewise represented that in line with the Company's vision to foster a culture where performance is recognized through differentiated rewards and personal development, NPI established the PSUP effective starting January 1, 2009, which was later amended on February 1, 2014, in support of the Company's "pay for performance" philosophy and provide an additional incentive to contribute to the value creation of Nestlé. Under the PSUP, **Performance Share Units (PSU)** are awarded to a restricted number of employees within the Nestlé Group.

The following provisions are found in the Articles of Nestlé Performance Share Unit Plan (PSUP):

ARTICLE 2

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Eligibility

2.1 The management of each Nestlé entity participating in the Plan shall propose Employees eligible to participate in the Plan. Such proposal shall be reviewed and approved by the CEO or the Compensation Committee of the Board of Directors of Nestlé S.A., as the case may be.

2.2 Neither the establishment of the Plan, nor the grant of Performance Share Units, nor the payment of any benefits nor any action of Nestlé shall be held or construed to confer any Employee any right to participate or to continue to participate in this Plan regardless of the length of time such Employee has been granted benefits under the Plan.

ARTICLE 3

Grant of Performance Share Units

3.1 The management of each Nestlé entity participating in the Plan shall propose the number of Performance Share Units to be granted to eligible Employees. Such proposal shall be reviewed and approved by the CEO or the Compensation Committee of the Board of Directors of Nestlé S.A., as the case may be.

3.2 The Performance Share Units shall be granted to eligible Employees free of charge.

3.3 The Performance Share Units do not entitle the Participant to any shareholder rights such as dividends payments or voting rights in relation to the underlying Shares until the Shares are transferred to the Participant pursuant to Article 5 (Vesting of Performance Share Units).

3.4 Performance Share Units are non-tradable and may not be sold, assigned, pledged, transferred or disposed of in any manner other than by will or by provisions of the applicable inheritance laws.

ARTICLE 4

Performance Share Unit Agreement

4.1 The award of Performance Share Units shall be evidenced by a written Performance Share Unit Agreement (i) specifying the number of Performance Share Units granted and the Award Date, and (ii) setting forth the terms and conditions applicable to such Performance Share Units.

4.2 The eligible Employee has the right to accept or refuse the award of Performance Share Units. Acceptance of such award has to be made in the manner and within the time period indicated by Nestlé. Should an eligible Employee not accept the award of Performance Share Units within such time period, it will be considered as a refusal of the Performance Share Units and shall result in such Performance Share Units becoming not granted, null

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and void.

4.3 The Performance Share Unit Agreement shall provide for any restrictions on the Performance Share Units or the issuance and resale of any Shares transferred to a Participant upon vesting of a Performance Share Unit that may be appropriate to ensure compliance with applicable securities laws.

ARTICLE 5

Vesting of Performance Share Units

5.1 Each Performance Share Unit shall vest on the day of trading at SIX Swiss Exchange following the last day of the Restrictive Period, except as otherwise provided in this Plan or any Addendum.

5.2 Upon vesting, Nestlé S.A. shall

i. Calculate, according to the Share Performance Criteria, the number of Shares resulting from the vested Performance Share Units; and

ii. Determine, in its sole discretion, whether such Shares or their Cash Equivalent shall be transferred, free of charge, to the Participant.

The payment of Cash Equivalent shall be made as soon as possible upon vesting. The transferred Shares shall belong to the Participant and are at his/her disposal.

5.3 Upon transfer of Shares to the Participant, he/she has to comply with the "Nestlé Policy on Inside Information." The current version is available on the Nest (NestléDocs).

ARTICLE 6

Termination of Employment

6.1 Upon termination of employment of a Participant as a result of death, redundancy, disability, retirement, termination without cause or divestiture, all Performance Share Units of such Participant shall vest at the date of termination of his/her employment with Nestlé.

6.2 Upon voluntary resignation or termination of employment for cause of a Participant, all Performance Share Units of such Participant shall automatically be terminated and become void, without any compensation, at the date of termination of his/her employment with Nestlé.

In reply, please be informed that Section 2.33 (A) of Revenue Regulations (RR) No. 3-98 provides that a final withholding tax is hereby imposed on the grossed-up monetary value of fringe benefit furnished, granted or paid by the employer to the employee, except rank and file employees, whether such employer is an individual, professional partnership or a corporation, regardless of whether the corporation is taxable

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or not, or the government and its instrumentalities except when: (1) the fringe benefit is required by the nature of or necessary to the trade, business or profession of the employer; or (2) when the fringe benefit is for the convenience or advantage of the employer.

The term "fringe benefit" means any good, service, or other benefit furnished or granted by an employer in cash or in kind, in addition to basic salaries, to an individual employee (except rank and file employee).

It is clear from your representation that the grant of PSU, either in Nestlé S.A. shares or its cash equivalent, constitutes payment of fringe benefits under Section 2.33 (A) of RR No. 3-98. Its grant, including when to grant and how many shares to grant per eligible employee, is within the sole discretion of the Company and subject to the following conditions, as indicated in the Nestlé Performance Share Unit Plan brochure:

a) The employee is a Nestlé Company employee at the date of the grant; and

b) The employee is holding an eligible senior management position.

Such being the case, the benefits under your PSUP are subject to the fringe benefit tax under Section 33 (A) of the Tax Code of 1997, as amended, which provides, as follows:

> "(A) Imposition of Tax. — A final tax of thirty-four percent (34%) effective January 1, 1998; thirty-three percent (33%) effective January 1, 1999; and thirty-two percent (32%) effective January 1, 2000 and thereafter, is hereby imposed on the grossed-up monetary value of fringe benefit furnished or granted to the employee (except rank and the employees as defined herein) by the employer, whether an individual or a corporation (unless the fringe benefit is required by the nature of, or necessary to the trade, business profession of the employer). The tax herein imposed is payable by the employer which tax shall be paid in the same manner as provided for under Section 57 (A) of the said Code. The grossed-up monetary value of the fringe benefit shall be determined by dividing the actual monetary value of the fringe benefit by sixty-six percent (66%) effective January 1, 1998; sixty-seven percent (67%) effective January 1, 1999; and sixty-eight percent (68%) effective January 1, 2000 and thereafter . . ."

From the above-quoted provision, NPI being the employer, is liable to pay a final tax of 32% based on the grossed-up value of the benefit granted, which represents the actual monetary value of the aforesaid benefit under your PSUP. Accordingly, the 32% tax is payable upon the delivery of the shares of stock or its cash equivalent.

Furthermore, Section 34 (A) (1) of the Tax Code of 1997, as amended, provides that —

> "(a) In General. — There shall be allowed as deduction from gross income

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all the ordinary and necessary expenses paid or incurred during the taxable year in carrying on or which are directly attributable to, the development, management, operation and/or conduct of the trade, business or exercise of a profession, including:

(i) A reasonable allowance for salaries, wages, and other forms of compensation from personal services actually rendered, including the grossed-up monetary value of fringe benefit furnished or granted by the employer to the employee: Provided, That the final tax imposed under Section 33 hereof has been paid.

xxx xxx xxx"

The following are the requisites for deductibility of business expenses from gross income:

(1) The expense must be ordinary and necessary;

(2) It must be paid or incurred during the taxable year;

(3) It may be paid or incurred in carrying on the trade or business;

(4) It must be supported by receipts, vouchers or documents. (see *Zamora vs. Collector, L-15280*, May 31, 1953)

For this purpose, it is clear that the deduction shall be made in the year when the related expense is incurred which in this case is at the time of the delivery of the shares of stock of Nestlé S.A. or its cash equivalent.

Such being the case, NPI can claim as deduction from gross income the grossed-up monetary value of the benefit that is furnished to its eligible employees under the PSUP, which is the value of the shares of stock of Nestlé SA at the time of its delivery to the executives participating in the PSUP, or its cash equivalent.

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
Commissioner of Internal Revenue

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