

VAT and Income Taxing Condominium Corporations in the Philippines: A Critical Analysis of BIR Revenue Memorandum Circular No. 65-2012 and 9-2013

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Introduction/Background of the study

On October 31, 2012, the Commissioner on Internal Revenue issued Revenue Memorandum Circular No. 65-2012 ("RMC 65-2012") declaring that all association dues, membership fees, and other assessment/charges collected by condominium corporations shall now constitute income payments or compensation for beneficial services it provides to its members and tenants, for income tax purposes. Moreover, association dues, membership fees and other assessment/charges collected by a condominium corporation shall be subject to value added tax since they constitute income payments or compensation for the beneficial services it provides to its members and tenants.

Further, Revenue Memorandum Circular No. 9-2013 ("RMC 9-2013") also declared the taxability of association dues, membership fees and other assessment/charges collected by homeowner's associations from its homeowners and other entities despite its tax exemption privilege under Section 18 of R.A. No. 9904, also known as the Magna Carta for Homeowner's and Homeowner's Association. The Memorandum Circular shall now impose a value added tax (VAT), percentage tax and income tax on such association dues, membership fees and other assessment/charges collected by homeowner's associations from its homeowners.

There is however a creative way for the homeowner's association to be exempted from the directive of the Bureau of Internal Revenue from payment of income tax, value added tax and percentage tax.

The conditions are as follow:

1. The homeowners' association must be a duly constituted "association" as defined under Section 3(b) of RA 9904;
2. The local government unit having jurisdiction over the homeowners' association must issue a certification identifying the basic services being rendered by the homeowners' association and therein stating its lack of resources to render such services notwithstanding its clear mandate under applicable laws, rules and regulations. Provided further, that such services must fall within the purview of the "basic community services and facilities" which is defined under Section 3(d) of RA No. 9904 as those referring to services and facilities that redound to the benefit of all homeowners and from which, by reason of practicality, no homeowner may be excluded such as, but not limited to: security; street and vicinity lights; maintenance, repairs and cleaning of streets; garbage collection and disposal; and other similar services and facilities; and
3. The homeowners' association must present proof (i.e. financial statements) that the income and dues are used for the cleanliness, safety, security and other basic services needed by the members, including the maintenance of the facilities of their respective subdivisions or villages.

Updates as of this writing reveal that on September 5, 2013, the

Regional Trial Court (RTC) of Makati declared invalid RMC No. 65-2012 which subjected a condominium corporation to VAT and income tax [1].

Moreover, the Court of Tax Appeals (CTA) has just recently ruled that condominium or association dues as well as other fees collected from unit owners are not subject to income tax and withholding tax [2].

Nevertheless, the Bureau of Internal Revenue (BIR) insisted on collecting taxes on condominium association dues on the ground that the tax court's decision did not touch Revenue Memorandum Circular No. 65-2012 issued in 2012 that imposed the taxes, referring only to old BIR rulings on a related issue. "Since the CTA did not rule on the validity of RMC 65-2012, therefore, it is the prevailing rule today and all concerned taxpayers are required to comply with the provisions of said RMC," as claimed by Kim Henares, Chief Commissioner of the BIR [3].

This paper will deal with a critical analysis of BIR Revenue Memorandum Circular Nos. 65-2012 and 9-2013 and determine their validity or invalidity.

Review of Related Literature

It is worth stressing the correlation between the imposition of the income tax and the value added tax for the purpose of generating revenues. In the imposition of income tax, a levy of 30% shall be charged for corporations on the taxable income. Taxable income is computed as income received (gross income) minus allowable deductions. In this set-up, charges are collected annually which is why corporations are given a wide range of creativity in thinking of a variety of allowable deductions as supported by official receipts. On the other hand, a charge of 12% value added tax (VAT) is imposed on the gross income received by the Corporation (as reflected in the output tax which is charged by the Corporation taxpayer to the end consumer). In this set-up, input VAT credit (value added taxes paid from suppliers by the Corporation taxpayer) may be availed by the Corporation taxpayer for purposes of computing the gross income. The collection of the VAT is done on a quarterly or monthly basis, which is why corporations are not given enough range of creativity for tax avoidance given the amount of time and considering that credits on input taxes are only limited to value

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added taxes paid by the taxpayer to its suppliers. Although the liability of the VAT is charged to the Corporation (taxpayer), such burden of payment may be shifted to the end consumer.

The above current set-up by the Bureau of Internal Revenue for collecting income tax and value added tax for corporations may be useful in rationalizing the need of imposing value added taxes in generating revenues [4].

It is also worth stressing the history of the Value Added Tax in the year 1918 where it was initially directed to large businesses, and not intended for non-stock, non-profit corporations.

On October 31, 2012, Revenue Memorandum Circular No. 65-2012 was issued by the Bureau of Internal Revenue clarifying the taxability of Association Dues, Membership Fees and Other Assessment Collected by Condominium Corporations. Accordingly, such Association Dues, Membership Fees and Other Assessment Collected by Condominium Corporations shall be subject to income tax, value added tax and percentage tax.

Subsequently, Revenue Memorandum Circular No. 9-2013 was issued on January 29, 2013 clarifying the Taxability of Association Dues, Membership Fees and Other Assessment Collected by Homeowners' Association. Consequently, Homeowners' Association in high-end villages such as Forbes Park and Dasmariñas Village may claim exemption from payment of income tax, value added tax and percentage tax, provided that they comply with the conditions set forth as follows:

1. The homeowners' association must be a duly constituted "association" as defined under Section 3(b) of RA 9904.
2. The local government unit having jurisdiction over the homeowners' association must issue a certification identifying the basic services being rendered by the homeowners' association and therein stating its lack of resources to render such services notwithstanding its clear mandate under applicable laws, rules and regulations. Provided further, that such services must fall within the purview of the "basic community services and facilities" which is defined under Section 3(d) of RA No. 9904 as those referring to services and facilities that redound to the benefit of all homeowners and from which, by reason of practicality, no homeowner may be excluded such as, but not limited to: security; street and vicinity lights; maintenance, repairs and cleaning of streets; garbage collection and disposal; and other similar services and facilities.
3. The homeowners' association must present proof (i.e. financial statements) that the income and dues are used for the cleanliness, safety, security and other basic services needed by the members, including the maintenance of the facilities of their respective subdivisions or villages.

On September 5, 2013, in an action for declaratory relief filed before the Regional Trial Court of Makati City Branch 146 by Petitioner First e-Bank Condominium Tower Corporation against the Bureau of Internal Revenue, the Hon. Presiding Judge Encarnacion Moya pronounced Revenue Memorandum Circular No. 65-2012 as having been invalidly issued. Accordingly, the Revenue Memorandum Circular did not only clarify an existing law, but changes its import and interpretation that in so doing it prejudices the right of the petitioner as a taxpayer. The issuance was arbitrary and in violation of the due

process clause of the Constitution. This pronouncement, however, does not yet constitute the law of the land, which gives the Bureau of Internal Revenue a chance to appeal such decision on the basis of existing procedural rules.

In a Court of Tax Appeals (CTA) Decision dated June 3, 2014 Re: Office Metro Philippines Inc. vs. Commissioner of Internal Revenue (CTA Case No. 8382), the Hon. Fabon-Victorino ruled that association/condominium dues, membership fees and other assessment/charges collected from the members of the Condominium Corporation, are merely held in trust and which are to be used solely for administrative expenses in implementing its purpose(s), viz., to protect and safeguard the welfare of the owners, lessees and occupants, therefore the same are not subject to income tax and to withholding tax. The decision, however, did not address the imposition of the value added tax. Neither did it address the validity of Revenue Memorandum Circular No. 65-2012. Nevertheless, this decision does not yet constitute the law of the land as the Bureau of Internal Revenue is also given a chance to appeal such decision on the basis of existing procedural rules.

Characteristics of a Good Tax Policy

As emphasized by Dr. Annette Nellen, author of 21st Century Taxation Articles and Blogs, the following guiding principles will be useful for analyzing any tax proposal at any size, degree, and level. The guiding principles will serve as frameworks in helping the author determine whether the Memorandum Revenue Circulars (RMC 65-2012 and 9-2013) are good laws or not.

Equity and fairness

"Fairness" means equal treatment under the law, equal treatment for those equally situated, and no discrimination among taxpayers unequally situated unless that discrimination is consistent with the purposes and principles of a sound tax system.

It bears to state the pertinent portion contained in Revenue Memorandum circular 65-2012, thus:

"This circular is issued to clarify the taxability of association dues, membership fees, and other assessments/charges collected by condominium corporations from its members and tenants.

Background: The Bureau has issued several rules exempting from income tax assessments/charges collected by condominium corporations from its members, on the ground that the collection of association dues and other assessments/charges are merely held in trust to be used solely for administrative expenses in implementing its purpose, i.e. to operate, manage and maintain the condominium project, to defray the costs of the condominium, and from which a condominium corporation could not realize any gain or profit as a result of its receipt thereof.

"In addition, the same rules exempted association dues from value added tax for the reason that a condominium corporation does not sell, barter, exchange, nor lease any goods or property and neither does it render any service for a fee, but merely implements the administration of the required services to collect the association dues from the unit owners pursuant to its corporate purpose(s) as trustee of the fund thereof.

Clarification: The taxability of association dues, membership fees and other assessments/charges collected by the condominium corporation from its members/tenants and other entities are discussed hereunder.

Income tax: The amounts paid in as dues or fees by members and tenants of Condominium Corporation form part of the gross income of the latter subject to income tax. This is because a condominium corporation furnishes its members and tenants with benefits, advantages and privileges in return for such payments. For tax purposes, the association dues, membership fees, and other assessment/charges collected by a condominium corporation constitute income payments or compensation for beneficial services it provides to its members and tenants. The previous interpretation that the assessment dues are funds which are merely held in trust by a condominium corporation lacks legal basis and is hereby abandoned.

Moreover, since a condominium corporation is subject to income tax, income payments made to it are subject to applicable withholding taxes under existing regulations.

Value added tax (VAT): Association dues, membership fees, and other assessment/charges collected by a condominium corporation are subject to VAT since they constitute income payment or compensation for the beneficial services it provides to its members and tenants.

As penned by Hon. Encarnacion Moya of the Regional Trial Court Branch 146, Makati City, RMC 65-2012 did not merely interpret or clarify the existing BIR Rulings, but in fact legislated or introduced a new legislation under the mantle of its quasi-legislative authority. The BIR Commissioner, under the guise of clarifying income tax on association dues, made RMC 65-2012 effective immediately. This passage contravened the constitutional mandate of due process of law.

It is deemed relevant to state the pronouncement of the High Court in the case of Commissioner of Internal Revenue vs. Court of Appeals, G.R. No. 119761, August 29, 1996 (First Division), as follows:

It should be understandable that when an administrative rule is merely interpretative in nature, its applicability needs nothing further than its bare issuance for it gives no real consequence more than what the law itself has already prescribed. When, upon the other hand, the administrative rule goes beyond merely providing for the means that can facilitate or render least cumbersome the implementation of the law but substantially adds to or increases the burden of those governed, it behooves the agency to accord at least to those directly affected a chance to be heard, and thereafter to be duly informed, before that new issuance is given the force and effect of law.

What is being stressed out is the failure to observe procedural due process where there is a full and fair decision making process before the government takes some action directly impairing a person's property.

However, the BIR Commissioner took its stand by relying heavily on Section 105 of the National Internal Revenue Code 1997 which states:

SEC.105. persons liable: Any person who, in the course of trade or business, sells barter, exchanges, leases goods or properties, renders services, and any person who imports goods shall be subject to the value-added tax (VAT) imposed in Sections 106 to 108 of this Code.

The phrase "*in the course of trade or business*" means the regular conduct or pursuit of a commercial or an economic activity, including transactions incidental thereto, by any person regardless of whether or not the person engaged therein is a nonstock, nonprofit private organization (irrespective of the disposition of its net income and whether or not it sells exclusively to members or their guests), or government entity."

In other words, the BIR Commissioner made an interpretation that association dues, membership fees and other assessments/charges collected by a condominium corporation are covered under the phrase "*in the course of trade or business*" therefore making these collections as being done in the regular conduct or pursuit of a commercial or an economic activity.

Let us analyze this in detail by defining the term "commerce." Bouvier's Law Dictionary defines commerce as "any single bit of the activity that amounts in sum to the economy." The most expansive meaning includes all forms of human endeavor, including work and non-work, production and non-production, ownership and non-ownership, that affect the economic life of humanity. The economic life is a period of a thing's profitability or the economy as a whole. In relation to the economic life, "profit" is defined as the sum value that is realized from and endeavor over a period of time for a going concern, which is the remainder of the income derived or accounted minus the costs and expenses paid or accounted.

An activity where one stands to obtain value, gain or profit is the essence of a commercial activity, hence the reason why an individual must contribute to the lifeblood of the government by paying taxes.

In an interview conducted with Mr. Jerry Borromeo, Building Administrator of KB Lepanto Condominium Unit Owners' Association, Inc., "association dues, membership fees, assessments and charges are being charged and assessed by condominium corporations just enough to defray expenses for the maintenance of the condominium building which includes janitorial services, garbage collection/disposal, security services, utilities for water and electricity for the common areas, repairs and maintenance of the building structures, and other similar services and facilities." In other words, such assessment for association dues and membership fees are only enough to defray the administrative expenses in implementing its purpose, i.e. to operate, manage, and maintain the condominium project, to defray the costs of the condominium, and from which a condominium corporation could not, in any way, realize any gain or profit as a result of its receipt thereof.

Therefore, the previous BIR Rulings exempting from income tax the assessment/charges collected by condominium corporation from its members on the ground that the collection of association dues and other assessments/charges are merely held in trust to be used solely for administrative expenses in implementing the purpose of the condominium corporation should have been the correct way of implementing the same, not to be subjected to income tax, value added tax or percentage tax.

The Court of Tax Appeals, in the case of Officemetro Philippines Inc. vs. Commissioner of Internal Revenue was correct in ruling that "Condominium dues are not subject to Expanded Withholding Tax (EWT)" relying heavily on the previous rulings of the BIR to wit: BIR Ruling [DA-(C-239) 612-09] dated October 19, 2009; BIR Ruling No. [DA-(C-182) 468-09] dated August 18, 2009; BIR Ruling [DA-(C-162) 427-09] dated July 31, 2009; BIR Ruling No. [DA-(C-032) 137-09] dated March 5, 2009; BIR Ruling No. [DA-(C-016) 079-08] dated July 28, 2008; BIR Ruling No. 018-05 dated September 16, 2005; BIR Ruling [DA-304-04] dated June 2, 2004.

Neither should a value added tax be charged on these assessment/charges collected by Condominium Corporation because there is no value added on the services as these assessments are only meant to defray the administrative expenses in implementing the purpose of the condominium corporation, neither more nor less.

Therefore, RMC 65-2012 does not only appear to be unfair, but also unreasonable and unconscionable.

Worse, high-end villages such as Forbes Park and Dasmariñas may validly claim for exemption by reason of the enactment of RMC 9-2013.

That is why a Senate Resolution No. 141 Directing the Proper Senate Committee to Conduct an Inquiry, in Aid of Legislation, on the Reported Need to Review the Inequitable Value Added Tax Imposed on Homeowner's Association and Condominium Dues was introduced by Senator Miriam Santiago, such Resolution is stated as follows:

"WHEREAS, the Constitution, Article 6, Section 28, states: "The rule of taxation shall be uniform and equitable. The Congress shall evolve a progressive system of taxation";

"WHEREAS, in an article published on Interaksyon.com dated 30 December 2012, the country's richest-those living in Forbes Park and Dasmariñas Village-have been exempted from paying the newly-imposed value-added tax (VAT) on association dues;

"WHEREAS, the exemption was made through a ruling handed down by Revenue Commissioner Kim Henares imposing 12 percent VAT on condominium dues;

"WHEREAS, according to the report, it was not clear why Henares, excluded the high-end villages from her order;

"WHEREAS, it was claimed that Henares merely followed the provision in Republic Act No. 9904 also known as the Magna Carta for Homeowners and Homeowners Association, enacted in 2010, which provided tax exemption on subdivision dues and even on the association's income;

"WHEREAS, Section 18 of R.A. No. 9904, reads: "Where the LGUs (local government units) lack resources to provide for basic services, the associations shall endeavor to tap the means to provide for the same. In recognition of the associations' efforts to assist the LGUs in providing such basic services, association dues and income derived from rentals of their facilities shall be tax-exempt: Provided, That such income and dues shall be used for the cleanliness, safety, security, and other basic services needed by the members, including the maintenance of the facilities of their respective subdivisions or villages";

"WHEREAS, it was reported, that a closer reading of the law shows that the exemption applies only where the LGUs lack resources to provide for basic services, which is not the case with Barangay Forbes Park, Barangay Bel Air, or even Dasmariñas Village;

"WHEREAS, the report concedes that parenthetically, the above provision can and should apply to condominiums, which are, come to think of it, vertical subdivisions; however, the Henares exemption of the subdivisions will allegedly have one unintended but unfortunate consequence-it will widen the already large gap between the association dues paid by Forbes residents and the monthly dues borne by lower-income condominium dwellers;

"WHEREAS, citing an example, the report claimed that Forbes Park and Dasmariñas Village residents pay only P23 a square meter every month in VAT-exempt association dues while unit owners of the lower middle-class DMCI condominium in flood-prone Pasig struggle with P35 per square meter plus 12% VAT in monthly assessments;

"WHEREAS, a large number of middle-class condominium buyers will not be able to afford the higher dues imposed on them in addition to their monthly amortization payments, especially since the VAT

ruling was implemented immediately;

"WHEREAS, the exclusion of affluent subdivisions is inconsistent with the State's policy to implement uniform and equitable taxation; it is also incompatible with inclusive growth;

"WHEREAS, there is a need for the legislature to amend relevant laws in order to abide by the Constitution's mandate for Congress to evolve a progressive system of taxation, and create a uniform and equitable system of taxation with regard to homeowners' association and condominium dues, taking into account the social class of those living in these guarded subdivisions and condominiums;

"WHEREFORE, be it hereby resolved to direct the proper senate committee to conduct an inquiry, in aid of legislation, on the need to review the inequitable value-added tax imposed on homeowners' association and condominium dues.

Certainty

Tax rules should specify when the tax is to be paid, how it is to be paid, and how the amount to be paid is to be determined. Basically, it is the level of confidence that exists that the tax is being calculated correctly.

This guideline can better be used to analyze the questioned Revenue Memorandum Circulars by making a benchmark on different countries in imposing value added taxes.

In Thailand, certain activities are exempted from the value added tax such as:

1. Small entrepreneur whose annual turnover is less than 1.8 million baht;
2. Professional services: Medical and auditing services, lawyer services in court and other similar professional services that have laws regulating such professions;
3. Income from business, commerce, agriculture, industry, transport or any other activity not specified earlier.
4. Services in the nature of employment of labour, research and technical services and services of public entertainers;

In Singapore a GST (goods and service tax, which is similar to the value added tax) of 7% is imposed. However, this rate is accompanied by an offset package to help Singaporeans with the increase in GST. The offset package would help the majority of Singaporeans offset their increased GST costs for several years. The offset package consisted of direct transfer benefits, in the form of cash payouts (GST credits, growth dividends, senior citizens' bonuses), central provident fund (CPF) top-ups (post-secondary education account top-ups for students, Medisave top-ups for older Singaporeans), and rebates (on utilities and public housing service and conservancy charges). Those who earned less or lived in smaller homes receive more benefits. The government also argued that the Workfare Income Supplement, a wage subsidy, would provide significant support for lower-income workers on a continuing basis even after the GST offsets have been distributed.

Regressivity is usually a greater issue for developing countries where a large proportion of the population lives in poverty. For this reason, many developing countries have adopted multiple VAT rates with the lower rates applying to necessities such as food and utilities as well as exempting a wide range of goods and services to promote greater progressivity. Empirical studies into VAT adopted in developing countries have shown that such measures do address the problems of

regressivity and make the tax more progressive [5].

In effecting RMC 65-2012 and RMB 9-2013, was there an initial study conducted before the same were validly implemented? Were there benchmarked studies conducted before the same was effected?

Convenience of payment

A tax should be due at a time or in a manner that is most likely to be convenient for the taxpayer. Appropriate payment mechanism depends on amount of liability and ease of collection.

It is a fact that real property taxes on condominium units are being levied, assessed and collected through the local government units in accordance with Section 38 and 39 of Presidential Decree 464, also known as the Real Property Tax Code. As a result, condominium unit owners (members of the condominium corporation) are required to pay their respective real property taxes as prescribed by law.

Although the payment of value added tax, income tax and percentage tax is imposed on the condominium corporation, the latter can nevertheless shift the burden of payment of value added tax to the members and tenants of said corporation. In the end, condominium unit owners (members of the condominium corporation) will eventually be charged taxes twice for the same enjoyment and use of their own real property, i.e. payment of real property tax on the real property, and payment of value added tax for the use and enjoyment of said property.

This scheme is in the guise of a double taxation which constitutes a huge burden to the members of the condominium corporation. This juridical type of double taxation happens when comparable taxes are imposed by two or more taxing jurisdictions on the same taxpayer in respect of the same taxable income or capital. This is in the form of economic double taxation. While there is no specific prohibition against double taxation in the fundamental law of the land, the 1986 Philippine Constitution requires that the rule of taxation be uniform and equitable to prevent undue discrimination and the imposition of excessive taxes. By implication, double taxation if allowed may violate public policy against excessive taxes [6].

No one should be levied a tax on himself or for himself. "Contributions to expenses" are simply these in reality; for, dues and assessments for common areas and other expenses for common utilities in the condominium are in reality expenses on and for oneself, as common areas are owned and are part of the "persona" of the condominium owners who collectively may hire a professional or an organization to help them manage their common ownership of the condominium per RA 4726, as amended [7].

Economy of collection

The costs to collect a tax should be kept to a minimum for both the government and taxpayers. This is closely related to the Simplicity Principle.

In a report prepared by Aure and Amurao [8], aggregate VAT revenues more than doubled from Php156.67 billion in 2005 (pre-RA No. 9337 regime) to Php330.78 billion in 2010. There was a sharp increase in VAT collection of both the BIR (60.42%) and the BOC (72.74%) in 2006, which was attributable to the first full year implementation of RA No. 9337, and the increase from 10% to 12% of the VAT rate. Specifically, the BIR VAT revenue showed an upward trend from Php80.22 billion in 2004 to Php173.28 billion in 2010 except for 2008 when collection dropped by 3.23% from the previous year's collection. The decline was traced by the BIR to the increased input tax

claims by importers and taxpayers with capital expenditures of more than Php1 million in 2007, and other non-recurring transactions such as privatization, audit/assessment, closures, etc., of about 8% of the total VAT collected (Table 1).

It is noted that since the full implementation of RA No. 9337 in 2006, the share of VAT to total tax revenue significantly increased from a 22%-23% level to a range of 28% to 30%. Hence, the passage of RA No. 9337 (i.e. broadened tax base, increased rate and the 70% cap on input VAT in 2005) has proven to be an effective revenue generating measure (Table 2).

Another way of assessing VAT performance is through the determination of its efficiency ratio or the ratio of VAT revenue to the VAT base divided by the standard VAT rate. For this purpose, the VAT base was represented by GDP and aggregate consumption expenditures. The use of these VAT tax bases are justified by the fact that the level of economic activities or GDP influences VAT revenue while consumption expenditures reflect the consumption type nature of VAT. Using the GDP as the VAT base, the ratio is known as VAT efficiency ratio or sometimes called VAT productivity. On the other hand, using the aggregate consumption expenditures as the VAT base, the ratio is known as Consumption Efficiency Ratio or simply C-Efficiency. An efficiency ratio of 100% is an indicator of a very good VAT system while a low ratio is typically taken as *prima facie* evidence of erosion either by exemption and zero-rating or by imperfect enforcement. In 2004 and 2005, the ratio of VAT to GDP was 2.86% and 2.88% respectively. Starting 2006, it went up to 4.31%; however, declining rates were noted in the succeeding years. Moreover, prior to RA No. 9337, the VAT efficiency ratio was about 29% using GDP as the VAT base. Since its full implementation in 2006, the VAT efficiency ratio improved to almost 36% although it continuously declined over the years until it reached about 32% in 2010. In the case of VAT efficiency with respect to aggregate consumption or C-efficiency ratio, a similar pattern is observed during the period under review (Table 3).

The possible reasons for the decline can be attributed to the complicated tax administration of the VAT and the broken VAT chain brought about by the passage of certain measures which have

| Year | VAT Revenues | | | Growth Rate (%) | | |
|------|--------------|--------|--------|-----------------|--------|-------|
| | BIR | BOC | Total | BIR | BOC | Total |
| 2004 | 80.22 | 58.88 | 139.10 | -2.92 | 11.81 | 2.81 |
| 2005 | 87.86 | 68.81 | 156.67 | 9.52 | 16.86 | 12.63 |
| 2006 | 140.01 | 118.87 | 259.80 | 60.40 | 72.75 | 65.83 |
| 2007 | 145.01 | 129.02 | 274.03 | 2.90 | 8.54 | 5.48 |
| 2008 | 140.32 | 156.33 | 296.65 | -3.23 | -21.17 | 8.25 |
| 2009 | 168.29 | 133.90 | 302.19 | 19.93 | -14.35 | 1.87 |
| 2010 | 173.28 | 157.50 | 330.78 | 2.97 | 17.63 | 9.46 |

Table 1: VAT Revenues and Growth Rates: 2004-2010 (Amounts in Billion Pesos).

| Year | Total VAT Revenues | Total Tax Revenues | %Share to Total |
|------|--------------------|--------------------|-----------------|
| 2004 | 139.01 | 598.01 | 23.25 |
| 2005 | 156.67 | 705.62 | 22.20 |
| 2006 | 259.80 | 859.87 | 30.21 |
| 2007 | 274.03 | 932.93 | 29.37 |
| 2008 | 296.65 | 1,049.19 | 28.27 |
| 2009 | 302.19 | 981.62 | 30.78 |
| 2010 | 330.78 | 1,093.64 | 30.25 |

Table 2: Share of VAT Revenue to Total Tax Revenues: 2004-2010 (Amounts in Billion Pesos).

negatively affected the flow of potential revenue from the VAT such as the passage of the National Grid Corporation of the Philippines Franchise, the Cooperative Code of 2008, and the Expanded Senior Citizens Act of 2010, as well as the effects of the global financial crisis.

It is worth noting that the average VAT efficiency and C-efficiency ratios in Asia and the Pacific region are 35% and 58% respectively while Keen pointed out that the average C-efficiency ratio on advanced and emerging markets is 50% although big variations were noted. On the other hand, the New Zealand Goods and Services Tax (GST), which is often held as a model VAT, has efficiency ratio of 65%. Hence, the Philippines' VAT efficiency and C-efficiency ratios are still below the Asia and the Pacific average and far from New Zealand's ratios.

Another important ratio that may show the efficiency of the VAT is the so called VAT gross compliance ratio (VATGCR) which is a measure of how well the VAT produces revenue for the government by taking into account the fact that the VAT is mostly applied to final consumption of households and individuals.¹⁹ In this regard, the VATGCR is the ratio of VAT revenue to private consumption in the economy divided by the standard VAT rate.

As shown below, VATGCR went up to 51% in 2006 or after the full implementation of the RVAT as compared to 41.5% level in 2004 and 2005 or prior to RVAT. However, VATGCR deteriorated beginning 2007 until it settled to 44.5% in 2010.

Overall, the RVAT regime in general is more efficient than pre-RVAT regime although it is still below the recorded average in Asia and the Pacific region. The highest efficiency ratio recorded in 2006 is due to the fact that the VAT coverage is at its broadest. VAT-registered taxpayers are limited to 70% input VAT credit and the rate increased from 10% to 12%. In 2007 onwards, the declining efficiency can be explained by the enactment of several measures exempting certain transactions from the coverage of VAT and the scrapping of the 70% cap on input VAT (Table 4).

Simplicity

A tax system is not unnecessarily complicated beyond what is

required of it to be consistent with the purposes and principles of a sound tax system. The tax law should be simple so that taxpayers can understand the rules and comply with them correctly and in a cost-efficient manner. It reduces the amount of errors, increases respect for the system and enables taxpayers to understand tax consequences of their transactions. The active business income of corporations is subject to a flat 30% rate for purposes of payment of income tax.

On the other hand, a 12% value added tax is imposed on any person who, in the course of trade or business sells, barter, exchanges, leases goods or properties, renders services, or engages in similar transactions and who imports goods. The value added tax is based on the gross selling price or gross value in money of the goods or properties sold or bartered. In computing the liability, the taxpayer subtracts from the tax due on sales taxes on his purchase of raw materials. He thus pays only the difference between the tax on sales (output tax) and the tax outlays for materials, supplies, services and capital goods (input tax). If at the end of any taxable quarter the output tax exceeds the input tax, the excess shall be paid by the VAT-registered person. If the input tax exceeds the output tax, the excess shall be carried over the succeeding quarters. Export sales are zero-rated.

Persons whose annual gross receipts do not exceed P550,000 are exempt from payment of value added tax but shall pay a percentage tax equivalent to three (3%) percent on quarterly sales.

Neutrality

This refers to the effect of the tax law on a taxpayer's decisions as to how to carry out a particular transaction or whether to engage in a transaction should be kept to a minimum. In this principle, taxpayers should not be unduly encouraged or discouraged from engaging in certain activities due to the tax law. Primary purpose of the tax system is to raise revenue, not change behavior.

The issuance of Revenue Memorandum Circular (RMC) 65-2012 by the Bureau of Internal Revenue (BIR) about two years ago led to the escalation of condominium living in the country, as association dues and fees paid by members and tenants of condominium corporations were made part of the gross income of the latter. Since the circular came into being, condominium corporations began collecting the 12-percent

| Year | VAT Revenues (BIR+BOC) | GDP at Current Prices | Consumption Expenditure | GDP | Consumption Expenditure | GDP | Consumption Expenditure |
|------|------------------------|-----------------------|-------------------------|-------|-------------------------|--------|-------------------------|
| 2004 | 139.10 | 4,871.55 | 3,838.83 | 2.86% | 3.62% | 28.55% | 36.23% |
| 2005 | 156.67 | 5,444.04 | 4,299.29 | 2.88% | 3.64% | 28.78% | 36.44% |
| 2006 | 259.80 | 6,031.16 | 4,819.43 | 4.31% | 4.31% | 35.90% | 44.92% |
| 2007 | 274.04 | 6,648.62 | 5,265.64 | 4.12% | 5.20% | 34.35% | 43.37% |
| 2008 | 296.65 | 7,409.37 | 5,978.73 | 4.00% | 4.96% | 33.36% | 41.35% |
| 2009 | 302.19 | 7,678.92 | 6,484.65 | 3.94% | 4.66% | 32.79% | 38.83% |
| 2010 | 330.78 | 8,513.04 | 7,077.14 | 3.89% | 4.67% | 32.38% | 32.95% |

Table 3: VAT Efficiency Ratio: 2004-2010 (In Billions of Pesos).

| Year | VAT Revenue (BIR+BOC) | Private Consumption | VAT Gross Compliance Ratio |
|------|-----------------------|---------------------|----------------------------|
| 2004 | 139.01 | 3,346.72 | 41.56% |
| 2005 | 156.67 | 3,772.25 | 41.53% |
| 2006 | 259.80 | 4,229.50 | 51.19% |
| 2007 | 274.03 | 4,611.88 | 49.52% |
| 2008 | 296.65 | 5,281.07 | 46.81% |
| 2009 | 302.19 | 5,674.97 | 44.37% |
| 2010 | 330.78 | 6,192.86 | 44.51% |

Table 4: VAT Gross Compliance Ratio 2004-2010 (Amounts in Billion Pesos).

value-added tax (VAT) on association dues paid by owners and tenants of such condominium units, hence, effectively increasing the cost of condominium living in the country [9]. Such increasing costs of condominium living will have the tendency of discouraging potential investors to buy a condominium.

Economic growth and efficiency

The tax system should not impede or reduce the productive capacity of the economy. In this principle, the tax system should be aligned with the economic goals of the jurisdiction imposing the tax.

In 2013 alone, 51,000 new high-rise units were unveiled based on the data released by property consultancy firm, Colliers International Philippines. This boom in the real estate industry may be attributed to affordable payment terms, according to National Real Estate Association Inc. president, Benigno Cabrieto. In an interview with the *Business Mirror* in February 2013, he said that low interest rates and Pag-IBIG fund have helped boost the condominium industry. Cabrieto mentioned that more Filipinos are now embracing vertical living because land is scarce and expensive. He also pointed out the increasing demand from Overseas Filipino Workers. Estimates show that 30% or P240-billion of the \$20-billion remittances was invested in real estate, mostly to condominiums in Metro Manila. The demand, he adds, is dictated by the need and affordability.

Indeed, should the value added tax be levied on association dues collected by condominium corporations, such increase will eventually decrease demand for investment in condominiums which in turn weaken the bullish growth of our condominium industry.

Transparency and visibility

This means that the tax system is transparent to the taxpayers so it is clear how much government costs and who is paying for it. Visibility is necessary for voters to determine effectively the amount and composition of government spending at which its benefits match its costs. Visibility is a key element in providing political efficiency.

VAT revenues are used to finance government's programs on education, health, environmental conservation and agricultural modernization. Furthermore, a fund called "*Katas ng VAT*" was used to provide a one-time subsidy to qualified senior citizens and lifeline users of electricity which directly benefited the poor. It also funded scholarships and loans to students, wives and relatives of transport workers, rehabilitation of areas damaged by typhoons and upgrading of provincial hospitals, among others. Moreover, VAT revenue shares of LGUs augmented their resources to finance basic social services.

Minimum tax gap

A tax should be structured to minimize noncompliance. Procedural rules are in place to attain compliance.

It should be noted however that the share of LGUs from the incremental VAT collections only accrues to the city or municipality where such taxes are collected and is allocated in accordance with the rule on the situs of the local business tax per Section 150 of the Local Government Code. Thus, the share may not be consistent and there are instances when some LGUs failed to avail of the said share because of complicated procedures involved in adopting the rule of situs of the local business tax, not to mention the absence of computer linkages in the VAT payment stations that makes it difficult for the BIR to monitor and verify the accuracy of the LGU's share from the gross receipts of business taxpayers maintaining branches, plants/plantations

or factories in different localities. Hence, only LGUs with incremental collection, with less complicated procedures in determining the situs of the local business tax and with computer linkages in the VAT payment system benefit from the said provision.

Appropriate government revenues

The tax system should enable the government to determine how much tax revenue will likely be collected and when. There is a need to have some level of predictability and reliability to enable governments to know how much will be collected and when. Generally, the government realizes better stability with a mix of taxes.

Tax research in the Philippines was institutionalized with the enactment of Republic Act (RA) No. 2211 (May 15, 1959) creating the Joint Legislative Executive Tax Commission (JLETC). Providing technical support to the Commission Proper was a Technical Staff which was formally organized on April 1, 1960.

When martial law was declared in 1972, the commission proper of the JLETC was dissolved. Recognizing, however, the vital role of a tax research institution in the overall economic development thrust of the New Society, then President Ferdinand E. Marcos, through the recommendation of the Presidential Reorganization Committee, decreed the conversion of the JLETC's Technical Staff to the National Tax Research Center (NTRC). On December 6, 1972, by virtue of Presidential Decree 74, the NTRC was organized as a purely single-headed agency under the administrative supervision of the National Economic and Development Authority (NEDA). More than a decade after, in another wave of government reorganization brought by the ascendancy of Ms. Corazon Aquino to the presidency in 1986, the NTRC was made an attached agency of the Department of Finance (DOF) by virtue of Executive Order No. 127 (January 30, 1987).

The National Tax Research Center (NTRC) is a government institution dedicated to promoting a tax system that will ensure a fair distribution of the tax burden among the Filipino taxpayers. It is bound to recommend necessary improvements in the tax system by conducting continuing quality research on taxation and to provide responsive staff support to fiscal policy makers.

As of this study, the NTRC has not yet released any research on the VAT Performance for the years 2011-2013. This output should have been useful in order to come up with a sound benchmark on how the Bureau of Internal Revenue may effectively implement RMC 65-2012.

Assessment and Conclusion

To summarize, Table 5 will analyze the current situation of RMC 65-2012 and 09-2013 using the Ten Attributes of a Sound Tax System:

Table 5 implies that both RMC 65-2012 and 09-2013 are not good tax laws for not having complied in 8 out of 10 Ten Attributes of a Sound Tax System. These memorandum revenue circulars not good tax laws because:

1. Assessment for association dues and membership fees are only enough to defray the administrative expenses in implementing its purpose, i.e. to operate, manage, and maintain the condominium project, to defray the costs of the condominium, and from which a condominium corporation could not, in any way, realize any gain or profit as a result of its receipt thereof.

| Attributes of a Good Tax Measure | Current Situation | Remarks |
|----------------------------------|---|----------------|
| Equity and Fairness | Senate 141 authored by Senator Miriam Santiago giving exemption privileges to high-end subdivisions. First E-bank Tower, vs. Bureau of Internal Revenue, Special Civil Action No. 12-1236, RTC Branch 146 Makati City, September 5, 2013. OfficeMetro Philippines Inc. vs. Commissioner on Internal Revenue, CTA Case No. 8382, Court of Tax Appeals Third Division, June 3, 2014. | Non-compliance |
| Certainty | Lack of initial study conducted | Non-compliance |
| Convenience of Payment | Provides additional burden to the unit owners Double taxation | Non-compliance |
| Economy of Collection | Efficiency Ratio and C-Efficiency Ratio is below the average Asia-Pacific Efficiency Ratio and the New Zealand Efficiency Ratio of 65% | Non Compliance |
| Simplicity | | Compliance |
| Neutrality | Tax burden discourages investors to buy condominium as the charges increase condominium living standards | Non-Compliance |
| Economic Growth and Efficiency | Weakens the booming economic growth of the condominium and high rise real property industry | Non-compliance |
| Transparency and Visibility | Beneficiaries are identified | Compliance |
| Minimum Tax Gap | only LGUs with incremental collection, with less complicated procedures in determining the situs of the local business tax and with computer linkages in the VAT payment system benefit from the said provision. | Non-compliance |
| Appropriate Government Revenues | No updated research studies on the effects and amount of collection by reason its implementation | Non-Compliance |

Table 5: Assessment of the Current Situation of RMC 65-2012 and 09-2013.

2. The revenue memorandum circulars are unjust and inequitable, therefore unconstitutional.

3. The revenue memorandum circulars did not merely interpret or clarify the existing BIR Rulings, but in fact legislated or introduced a new legislation under the mantle of its quasi-legislative authority. The BIR Commissioner, under the guise of clarifying income tax on association dues, made RMC 65-2012 effective immediately. This passage contravened the constitutional mandate of due process of law.

4. There is no valid classification as there is failure to distinguish condominiums (which can be classified as vertical subdivisions) from other high end subdivisions (such as Dasmarinas Village and Forbes Park) as the latter are exempted from paying income taxes and value added tax.

5. In effecting RMC 65-2012 and RMB 9-2013, there was no proof of initial studies conducted before these laws can be validly implemented. No benchmarked studies were also conducted before the same can be effected.

6. There is failure to observe procedural due process where there should have been a full and fair decision making process before the government takes some action directly impairing a person's property.

7. Since real property taxes on condominium units are already being levied, assessed and collected through the local government units in accordance with the Real Property Tax Code, an additional assessment of income tax, value added tax and percentage tax on association dues for condominium corporations will eventually result to double taxation, i.e. charging taxes twice for the same enjoyment and use of their own real property.

8. The laws are in the form of economic double taxation which violate the public policy against excessive taxes.

9. This tax burden discourages investors to buy condominium as the charges increase condominium living standards.

10. These tax laws weaken the booming economic growth of the condominium and high rise real property industry.

The concept of double taxation can be inferred from the revenue memorandum circulars. Since double taxation is frowned upon because the same is burdensome, it is recommended that these revenue memorandum circulars should be nullified in its entirety and should be set aside. A legislative enactment providing a clear imposition of income tax and value added taxes on condominium unit owners association should be the proper remedy.

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